LIVE ARTICLES ON SURETYSHIP

No. 2

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ON

SURETYSHIP

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FOREWORD.

To those who have read the first volume of "Live Articles on Suretyship" no explanation of the purpose of the present volume is necessary. It is not out of place, however, to repeat that the articles here presented, which were originally published in the monthly Suretyship Supplement of THE WEEKLY UNDERWRITER, were written for the purpose of instructing the men in the field in the technical points of the surety business with which they should be familiar. There is no limitation, nevertheless, of their applicability to the man in the home office, and it is hoped that the book will be found useful by him as well. In extending herewith their thanks to the contributors to this the second volume in the series, the publishers bespeak for them the same welcome that the first volume received.

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FRATERNAL SURETYSHIP.

Close Study of Corporate Laws—Knowledge of Membership and Methods Necessary to Correct Suretyship.

By Joseph R. Adams, Special Agent, American Surety, Chicago, Ill.

Fraternal sureties are as varied as are the organizations. Beneficiary societies do not encompass the field. Each individual brotherhood and each sisterhood come properly within the classification. Correct suretyship means a peculiar application to the individual body. To make such application it is important to have an intimacy with their laws, a sense of their aims, a knowledge of their membership, a plan of each chartered territory, a fraternal relationship with each governing body. Few corporate surety companies possess this acquaintanceship, consequently it is a business but little understood.

The increased attention and growth of fraternals reflect the importance of the subject. It is necessary that we establish a position, with a promise to make brotherhood of man more than a mere empty phrase. It must be a proposition to minimize waste and to exalt the functions of such bodies. We must accept them upon their own declaration, organizations calling forth the best effort of the individual and by such effort the raising of the standard of citizenship.

> "To protect the wage workers and institute better conditions with the assistance of progressive, intelligent combinations, therefore, in order to emancipate our fellow craftsmen from the oppressive burdens they are now suffering under."
>
> "We are bound together, not to shield or countenance wrong doing, but to assist each other in distress, help each other in want, counsel each other in difficulty."
>
> "To promote social culture, moral improvement and extend benevolence among its members."
>
> "To maintain and promote the interests of Americans, and shield them from the depressing effects of unrestricted immigration; to assist them in obtaining employment and to encourage them in business."

And this from a large international fraternity:

> "To gather into one mighty fraternity worthy men who appreciate the true meaning of friendship; who are cautious

in word and act; who love truth; who are brave in defending right; whose honor is untarnished; whose sense of justice will prevent a personal act or word injurious to another; whose loyalty to principle, to family, to friends, to their country, and to the constituted authority under which they enjoy citizenship is undoubted."

Under such enunciations it would appear that fraternal sureties must be placed in a preferred class of fidelity undertakings.

We may gather then that a fraternity is the child of American spirit and life. Teaching loyalty to established government, and obedience to law, upholding that governments are made for man and that the citizen who controls himself, who recognizes the rights of, and has faith in, his fellow citizens is the best prop and support of such a government. The history of fraternities is interwoven with that of this nation and of the English speaking race.

DATE BACK TO ANTIQUITY.

Fraternals are not fads, are not of the passing follies, are not something of this era only, for they are of great antiquity. Even to the uttermost recesses of the earth may be found the Masonic fraternity, an organization proud of its having been founded in the days of Solomon. Freemasonry was originally a fraternity of practical builders and they are credited with having entered into the construction of the house Solomon was about to dedicate to Jehovah, in the remotest ages of the earth. Knighthood, constituted bodies of Knights, dates back to the days of the Crusaders. The order of the Knights of Pythias claims inspiration from David, the beloved, and from Jonathan, his friend, youths of early Bible date.

Practically, fraternal organizations were given birth with the establishment of the Merchants' Guilds, under which towns were incorporated for trading purposes. And herein was a waste of competition. Their idea was the promotion of fair dealing, fraternal relations among themselves, a regard for the interests of trade, abolishing individual gain for a mutual interest.

Then came the Craft Guilds for their mutual interests, the promotion of honest work and fraternal relations. With the loss of the monopoly privileges these guilds once had they began to lose prestige and continued to exist and do now exist as social or mutual benefit societies. It is thus proven that man is diligent to his individual interests. He is not necessarily steeped in selfishness, but self is paramount. Considering his interests he attaches himself to social groups, his church, his union, club and fraternity.

Solidarism, which is opposed to Socialism and capitalism, was recently proposed by a Chicago Judge. "Even labor unions are

capitalistic in principle, caring only for their own interests," he said. "Solidarism is the term adopted to express mutual co-operation, in which everyone will seek the welfare of all without adopting the revolutionary extremes of Socialism."

Thus is shown that while fraternities may be varied and are many, all have the same fundamental principle and must be considered under the rules of adapted suretyship. The development of a proper legal system is often necessary, old premises must be discarded, as new situations are formulated. Previously allowed to operate as their governing officers ruled, many present day fraternities and especially so the fraternal benefit societies, must now comply with laws formulated for their guidance and obedience. For every radical change that is discountenanced by a better knowledge, numerous minor changes appear, proving that as yet the beneficiary organizations in their systems are awry. It proves, too, that the beneficiary societies are undergoing an evolution; an evolution that will result in better conduct, larger returns for expended effort, wiser usage of advantages. Man will grow better and fraternals will grow better as the conditions of their economic life become more acceptable.

STRICT CONTROL OF FUNDS.

It is obvious that there must be a proper suretyship, that there is necessity for a strict control of the funds of these organizations. What is rather to be insisted upon is that the lessons of the past shall be taken to heart by those charged with the conduct of affairs, so that noticeable mistakes and losses may be eliminated. What one weak, misguided officer might have done and the wrong condoned involves a disregard for individual integrity, weakens the force of argument, retards growth and the ultimate desire and success of an organization. This disregard, carefully considered, would be to raise the cost of membership and of maintenance. Full weight must be given to the undoubted truth that foes without, competitors, and foes within, unscrupulous members, obstruct in many ways to the extent that the system of accounting and discharge must receive careful consideration, obtained and sustained by a careful, abiding and understanding suretyship.

In the nineteenth century, in the United Kingdoms, labor organizations were criminal conspiracies, under both common and statute law. It was not believed under the trade union acts that they were liable for the tortious acts of their officers or members. It is a suggestive fact that laxity of conduct of some, not all, officers of beneficial orders has resulted in a wrongful abuse of confidence and a nefarious plunder of the trust funds, many and minor contributions from members in modest financial circumstances. And the grafting officers went

scot free under a law of fraternity, wherein no brother can do a wrong, a law fortunately that is rapidly disappearing and a new acceptance made, that an officer must be proven.

The efficacy of suretyship is shown in a more zealous knowledge of and adherence to the laws, thus minimizing acts of dishonesty, of negligence and carelessness. Suretyship educates a more sympathetic appreciation of duty as well as what is due to others, their rights and their interests. It is an equalizer between officer and member.

One of the most important aspects of the work of fraternal organizations, be it trade or beneficial, is the educational. By bringing together the members questions of common interest are discussed and an intelligent and broader insight obtained of various and varied subjects. The experience gained by the officers of these gatherings assists them to perceive the value of their daily pursuits. In consequence these officers are leaders. They are by nature constructive, possessed of a superior ability, commanding the respect and esteem of their associates. A fraternity is a miniature democracy. It begets the modification of personal opinions to the expressions of a majority. It is a mental and moral training for a higher and more useful citizenship. What perhaps is lacking is a satisfactory gauge, how is the desirable organization to be distinguished.

That organization which is placed the more truly upon a strict business basis must be the one more nearly desirable. The last several years have brought clearly into notice the fraternities worth while; fraternities showing advance in a conservation of their finances. By the adoption of surety bonds, a causative agent. By suretyship a recognition of a preventive of failure. Through such an agency the most pressing reform of organizations. A prerequisite of stability, of worth.

RECOGNITION OF SURETYSHIP.

Internal criticism accompanied the fraternal adoption of corporate suretyship. Yet it is gradually assuming its proper place. There is a growing recognition of its protecting influence. It has established a confidence in fraternities which is supreme. Buried in the graves of clever leaders are personality, cupidity, the evil so long and so patiently submitted to—ignorance. Truly years of fraternal waste. We might call them years of constructive fraud. Constructive fraud is known in law as such fraud as is involved in an act or contract which, though not originating in any evil or fraudulent design, yet has a tendency to deceive or mislead other persons, or to violate public or private confidences, or to impair or injure public interests.

Fraternal beneficiary societies were the first of the fraternities to make appreciable use of surety bonds. Adoption was made in the Middle West, where these particular organizations have

their greatest number. No less than a half dozen heads of fraternal societies lay claim to having presented the bonding idea to their associates, by a first adoption on their own officers. We are inclined to credit the first society service to an attorney, who, having had other dealings with a surety company and having had more or less petty annoyances from erring subordinate officers, presented a crude working plan, which was accepted. To-day few fraternal beneficiary societies would do without corporate suretyship.

The original bond form was a sad commentary upon the carefulness of the surety supply man. The form excelled in two particulars. It was as long as the moral law and it had an ingenious shuffling of whereas and whereats. Succeeding paragraphs of the form completely nullify the paragraph preceding. Manual rates were not in force at the time. No experience had been had. The line was taken on at any ancient rate. There is a curious old bond form in an Illinois fraternal office. The instrument is measured in feet. It has a schedule attached. The premium rate was ninety cents per each thousand dollars of liability. About all the society received in return for its premium were promises and a roll of printed paper. The instrument was one of the pioneer variety, practically cancelling its own obligations. Where the verbiage did not succeed the surety company did. At that, the carrying company had really earned its premium in the work performed. Applications were necessary and several hundred applications upon individual risks of from one to two hundred dollars soon offset amount received.

The surety companies and the fraternities both became wiser. The result, proper bond forms and proper rates.

Previously was mentioned a thought that fraternal sureties might be placed in a preferred fidelity class. That would be only partially true. There are both the desirable and undesirable risks, the same as in all lines. The long, wordy bond form has been displaced by a model of brevity. In fact there are three fraternal bond forms, varying in the obligations assumed under the suretyship. Applications have been waived, up to a certain individual liability. On minor amounts the office and not the officer is under the bond. This arrangement would apparently increase the liability. It is not necessarily so. If the surety takes the precaution to advise itself of the character of the fraternity and the class of men or women accepted into membership. If the organization is of good grade, its officers having passed the ordeal of inspection and acceptance into membership, application, inspection and recommendation have come through that method to the surety. As a usual proposition the members of a fraternity are neighbors, have long known each other, it is a community affair and the electing lodge body has an acquaintance with its officers that no surety could possibly obtain.

Should the organization be sub-standard, and there are many such, their liabilities are far from being desirable. Dangerous and prohibitive.

LIBERAL FORMS USED.

The present form of fraternal bonds are liberally broad. Within the liability not only a guarantee of personal honesty, but also acts of omission, performance of duties, absolute accounting for funds and securities, even embracing depository features.

There is a distinction made in the rates between societies composed of men, and men and women, and those wholly of women. Experience justifies the statement that there should be no distinction. Rates should be uniform. It is possible that the surety rate making body was actuated by sentiment. It is the experience that the men's order shows more losses by peculation, women's orders show more losses through lack of business understanding. As between the two classes, men and women's societies, the ratio of losses are about equal. On salvage the men's societies far exceed women's societies. In fact, the loss on a woman is practically net. Woman is confiding, lacks the sensibility of danger. She is inclined to intrust her money to the bureau drawer, easy of access. Through women's trustfulness many a loss has been discovered, a shortage in amount on the day of settlement. Interesting incidents of women's losses might be related, because of woman's innocence. One such narrative will suffice. A matronly lady was elected as the treasurer of a local lodge. At a regular audit the lodge money was found short. A demand was made upon the officer and she stated she was not short, that all bills presented for payment had been promptly met. That when she was elected and assumed the office, she had been informed that her duties were to pay all bills approved and that any and all amounts in excess would be hers. Loss was reported to the surety company. An investigation was made. The treasurer was found to be a mild mannered, soft voiced, elderly Scotch woman. A look at her face, at her humble and yet scrupulously neat little home, and her rehearsal of her side of the case, stamped in unmistakable language—no wrongful intent. There was no possibility of salvage. The surety swallowed the loss and made request that another officer be elected. But be it said for these strictly women's organizations that their superior or supreme officers are women of great business ability. The women's orders of the United States are remarkable for their size, and for the large treasury amounts they possess. Several of the orders have fine headquarters. An analysis of their investments shows the same to be of a gilt edge character, first mortgages

and high class bonds. Another evidence of woman's astuteness is this, few if any women's organizations are without surety bonds.

INCREASED RESPONSIBILITY.

The beneficiary fraternities, now that they are coming directly under the exactions of the insurance departments, as to solvency, and are to be held in strict compliance of contract, must of necessity become more dependent upon the inspection and supervision of surety. The fraternities were conceived in friendship. They were mutual organizations of relief among selected acquaintances. They originally had no intention of a long existence. As such they were crude, had little need of laws of conduct and no necessity of accumulations. They were made up of those of an equality, as to station in life and in financial condition. Some fraternities were of a family character, blood relatives. One such fraternity continues, after an existence of more than a century of time. Commercialism entered finally. Paid solicitors were employed. The fraternals became national in scope. Liabilities and income rapidly widened. Certain concerns failed and the most of the beneficiary fraternities were threatened. Then stepped in the law. The year nineteen hundred and eighteen marks the half century of the beneficiary organizations in the United States. In a badly dismembered condition, the original order exists. During the half century more than $3,000,000,000 have been paid out in death and sick benefits. The present liabilities under the certificates of membership, estimated 9,000,000, exceed $10,000,000,000. At the beginning of 1917 the assets of all American fraternal beneficial orders was but a third of the booked liabilities, or $313,000,000. The full collections for the preceding year were $173,000,000; disbursements $129,000,000 Think of it, $10,000,000 weekly paid out by such organizations alone. The need of surety protection must be apparent.

Every creed, sect and race enters into beneficiary organizations. Certain fraternals refuse membership to those outside church or race. Observation develops that fraternals, distinctly church or distinctly race, German, Jewish, Scandinavian, Polish, Slavonic, Bohemian, and there are several of each, are more careful in a demand for corporate suretyship. They are insistent that there be a sufficient amount of surety and that each financial officer be bonded. The composition of membership is principally of the middle or laboring class. Naturally they are frugal. Statistics prove that these assessment orders have reduced pauperism in the States, thirty-three per cent.

Proper classification and the correct application of rates demand carefulness on the part of the underwriter. The manual is not always easy of interpretation. It has been known that

benevolent and church fraternities, because they operate under certain affiliations, being given the rate applicable to such connection. Not taking into consideration the extent of their chartered privileges, which invariably they exercise, the writing of certain forms of insurance. Other organizations, largely trade, provide help for the needy, sick and dependent member and bury their dead,—not strictly beneficiary. Their rates differ. Purely benevolent, educational, religious, semi-public institutions have their classification.

THE SURETY HAZARD.

Constitutions and laws, governing the various fraternities, while similar in a general way, are framed individually. A lack of a knowledge of the laws is the threat to surety. Fraternity laws are subject to and more often undergo changes at the periodical sessions of the governing body. Liability under suretyship is largely governed by these laws. It is an unpardonable grievance and an unmistakable fact, many head officers of fraternities do not know their own laws. Consequently their administration is at fault. Other officials, while knowing their laws, fail in performance. In the latter case the subordinate officials become neglectful, fail under their duties of office and while, perhaps, not criminal in act, occasion numerous and annoying losses. To know and interpret and to obtain compliance is the educational act of the surety.

Surety companies have not been solicitous for fraternal business because of the many details involved. Agents and brokers have accepted, but have not pursued such bonds because the individual risks have been very small and the premiums of a minor amount. The fraternal leaders, the officials, have prejudiced their own surety arrangement by failing to give the assistance expected. They should simplify their laws and know the same and should insist upon a complete understanding and observance by subordinate officials. When the men higher up wink at failure, fearful of their own political existence and retention of office, little can be expected of the subordinates. Failure has aggregated fraternal claims, has made accumulated liabilities. The penalty of removal from office on discovery of a loss is not sufficient. A willful wrong should be punished by a dismissal from membership. A repetition of the Chinese law for bank failure, the head of the offender.

Suretyship is no longer an open question with fraternities. It is a growing necessity, a fixed part of their system. It is stronger than cupidity, more powerful than selfishness and beyond sneers or scowling ignorance. Its adoption was the step that was necessary toward a practical realization of the hopes of those who believe that these beneficiary organizations will

provide an estate when the payor has ceased to live. Fraternals have a great moral, as well as financial, obligation. Our national honor may be said to be involved in the proper handling of the immense trust funds. Suretyship is the wireless system that sounds the S O S, when the small lodge is foundering; when the unwise officer has betrayed his obligation.

FLEXIBILITY OF CORPORATE SURETYSHIP.

Admirable Adaptability of This Form of Protection to Meet New Demands of Modern Business.

By E. D. Livingston, Superintendent Bonding Department, Roval Indemnity Company.

Every day the surety underwriter is called upon to solve some new problem and adapt corporate suretyship to some new requirement for security, which may grow out of a single and unusual contract or be required to meet a general condition. The surety bond is flexible and may be used to meet practically any such requirement, and the resourceful surety underwriter is generally able to arrange such surety bonds without exposing the bonding company to any undue hazard. A real and indispensable service is afforded by corporate suretyship which could be fully appreciated only in the event of its discontinuance. The constructive work which has been accomplished in a few years forecasts a wonderful future development. The men who are making corporate suretyship their life work have the satisfaction of knowing that they are building an institution which is and will continue to be regarded as an essential.

Many established lines of the present were a short time past unusual and experimental and many of the new lines of to-day will to-morrow be undertaken as a matter of course. And so the institution of corporate suretyship has grown and will continue to grow to meet changing conditions. Surety bonds are being used to take care of requirements for security which were heretofore taken care of in some other way or not at all.

A striking example of the ready response of the bonding companies to the requirements for security is the title guaranty bonds which are now issued to the Federal Land Banks. Federal farm loans are provided for by an act of Congress to aid farmers by enabling them to borrow money on a long time mortgage and to amortize the loan. The farmer who can arrange such a loan will not be bothered by mortgage renewals and consequent risk of foreclosures for non-payment of principal. It is generally conceded that this is an excellent scheme for farmers generally to whom its advantages, as to the country generally, are obvious. A security known as farm loan bonds is issued against such mortgages, and these bonds are considered an excellent investment. The plan of operation is conservative as to appraisement of property and the margin of value in ex-

cess of the amount loaned. There is one factor which must always be considered in lending money on a real estate mortgage, and a most important one, namely, clear title of the mortgage to the property. Some of the farm loan banks felt that the farm loan bonds would be much more attractive as an investment if the title to the mortgaged property could be guaranteed. The mortgagor, of course, primarily guarantees the title but a further guarantee seemed desirable. The title guarantee companies were not in a position to furnish such security. Their plan of operation is not sufficiently flexible to assume such risks. The demand for this security grows out of the obligation on the part of the farmer. who is borrowing the money, to hold the land bank harmless in the event of a defect in title. This requirement for security has been met by the bonding companies. I am reliably informed that practically all of the farm loan banks are considering the bonding companies' plans and that the last report showed that five or six of the banks have already accepted surety companies' bonds which hold the lenders harmless in event of defect in title to the mortgaged property. It is in many ways fortunate for the success of the land bank scheme that the bonding underwriters have found a way to satisfactorily meet this condition. The agreement between the lender and the borrower underlies the security bond and it is out of that agreement that the requirement for security arose.

Another striking example of the response of the surety companies to a requirement for security growing out of an agreement, is the automobile embezzlement bond. Automobile dealers generally sell motor vehicles on the partial payment plan, the dealer retaining title to the vehicle until paid for. Heretofore, the dealer has secured fire and theft insurance under which the insurance company has assumed liability in event of the theft of the car by the purchaser. Recently some of the States have required fire companies to discontinue covering the embezzlement feature. Dealers' collateral frequently consists only of the car, and the hazard of loss by theft of the purchaser is, as we have found, an actual hazard. Some surety companies are now issuing what are known as automobile embezzlement bonds, indemnifying the dealer against the loss of his car caused by larceny, embezzlement, conversion or criminal misappropriation by the purchaser. The local dealer would be in a position to so regulate his credits that this requirement for security could be waived, but when it becomes necessary for him to hypothecate the paper, such paper can be more readily disposed of if it can be shown that if the note is not paid by the purchaser the car can be repossessed by the dealer and resold by him for an amount sufficient to take care of the balance of the purchase price. The dealer can arrange for such insurance that he would be reimbursed for a loss on account of anything which might

happen to the car or on account of the disappearance of the car. It is the opinion of the large automobile finance companies that the bonding companies have again proved, by taking care of this requirement for security which could not be met by any form of insurance, that they are indispensable to the welfare of the business world.

In the early part of 1916, on account of the U-boat warfare, it was considered dangerous to transfer securities from Europe to this country. Securities had been lost on the steamships *Titanic* and *Arabic* and in order to secure a duplicate issue, it was necessary for the applicants to satisfy the bonding companies that the securities had actually been lost so that the bonding companies could issue bonds required upon duplicate issue of securities. The problem was solved in a very ingenious way. I quote from a bulletin issued by the Towner Rating Bureau under date of March 31, 1916:

"Foreign bankers and their American correspondents can solve the problem of transferring securities from Europe to this country in the following manner:

"The American securities which it is desired to transfer, will be marshalled at a convenient point, and there burned in the presence of a representative of the European bankers, their American correspondents, the American consul, and the surety company. The name of the owner, the serial number, and an accurate description of each security, will be certified by those present and its destruction duly attested.

"On receipt in this country of such certificate and attestation, application may be made for a reissue of the securities thus destroyed; and such securities will be reissued on the usual indemnification of a surety company's bond, as for 'Lost securities.'

"This method will avoid seizure of securities by the enemy, and will save insurance premiums now charged for trans-Atlantic shipments."

This arrangement is another striking example of the response of surety companies to an unusual requirement for security; and is evidence of the flexibility of corporate suretyship.

When I read order No. 25, issued by the director general of railroads (which order gives the railroad companies the right to extend credit for freight for forty-eight hours after the delivery at destination), I wondered how the railroads and the shippers would have regarded such order if corporate suretyship were not available. Under the order, it would have been necessary for the debtor to have filed a private surety bond, and modern business institutions, as a rule, are not favorably disposed toward the acceptance of a private surety bond. When the debtor files a corporate surety bond issued by a company

satisfactory to the railroad, the acceptance of the bond becomes a mere detail and saves the railroad time and trouble in investigating and determining the sufficiency of a private surety. No matter how large the financial responsibility of the debtor, it would have been inconvenient for him to have secured private surety. This arrangment by the director general of railroads provides an undoubted convenience to the debtor, but before such convenience could be availed of the requirement for this security had to be met.

Many a business transaction has reached a point where for want of security it failed of consummation. Business men are very apt to think of a surety bond when certain loose ends of a deal cannot be tightened in any other way. The surety underwriters are becoming better equipped each day to deal with unusual propositions.

It will be for the general good of corporate suretyship when all local insurance agents become surety underwriters. The local insurance agents of this country include many of the most substantial men in their respective communities and form an army of men of superior intellects. Suretyship is a branch of the insurance business, an important branch; it needs the constructive ability of the entire insurance fraternity and I am confident some day will have it. It is my firm conviction that if all insurance agents realized the possibilities of corporate suretyship, realized the great chances for constructive work and for devising ways and means for facilitating general business intercourse, they would speedily become equipped to deal with suretyship problems.

The term "surety underwriter" embraces all agents who determine the desirability of a surety risk and those who are able to collect data and arrange for the security of a bonding company, whether such underwriters are located in the head office or in the field; thousands of local agents are in a position to qualify as surety underwriters to-day. Owing to the peculiar nature of the business, its success depends largely upon the intelligence and loyalty of the companies' agents. The past success of the business proves conclusively that it has attracted men of high calibre and will continue to attract such men who can make the most of the flexibility of corporate suretyship.

PERSONAL SURETYSHIP INSECURE.

A Glittering Mirage That Disappears on the "Show Down"—Rules of Courts and Practise of Law Against the Personal Surety.

Address Delivered before the Surety Underwriters' Association of Chicago, May 7, 1918, by William R. Medaris, Attorney, National Surety Company, Chicago.

The claim department of an insurance company is a more or less sordid place, and it is very good for us to meet occasionally with the underwriting branch of the business that some of the splendid optimism of the men who write insurance and bonds should come to leaven the loaf of the men who meet nothing but trouble.

I suppose the reason why so few people are ever promoted from the claim department to the agency field (and you will note I say "promoted") is that if it were left to the claim men, they would never write a bond or execute a policy. They could always see how they were going to lose, but never how they were going to win. By the time a man has spent a few years in the claim department, he will have lost some of his optimism. His vision by then is likely to be backward rather than forward, and his volition will be largely controlled by experiences which tend to tether him to the stake.

In suggesting a topic for this task, however, it occurred to me that the underwriters might be interested in hearing something about what goes on with some cases after they are through with them, after they have collected the premium, if they have, and have forgotten the incident.

INSECURITY NOT SURETY.

And one of the most glittering of all mirages, the thing that fades away into nothingness—just as you want to use it—is the personal indemnity agreement; and so I thought it would be a good thing for me to tell you some of the things I have learned about personal indemnity as security, or rather, the insecurity of personal indemnity.

I had an uncle once that was a kind of money lender around in the neighborhood where he lived, and he had a reputation of being a wonderful collector. When Uncle Bill got a hold of a bad one his system was something like this: He would meet his debtor on the street—very casually, of course—but also very

soon after the note was due—and he would say, "John, your note was due the other day, did you forget it?" Then would come some camouflage on the part of John, and Uncle Bill would say, "Several of the boys thought I was very foolish to loan you that money, John, but I said to 'em, says I, 'No, sir, John is as honest as the day is long. I'd trust John with anything; his word is as good as his bond with me any day.'" Now something about the way he put his man on his honor usually got the money. It was his very confidence in the man that brought the response. There was no "rough stuff" about Uncle Bill, he just let the fellow know that he had trusted him and he expected him to pay, and in most cases it worked. At least it worked much oftener and much more quickly than a lawsuit in Chicago.

The point about this story is just this—that the security in personal indemnity rests largely upon the ability of your salvage department to make the fellow "want to pay." If it is unable to make the indemnitor want to pay, the chances of being able to "make him pay" are no more than fifty-fifty, and this is true even though he is able to pay. Two things are absolutely essential to the security furnished by the personal indemnity—a desire on the part of the indemnitor to pay and his ability to pay, and of the two the most essential is his desire to pay.

PERSONAL SACRIFICE.

Have this in mind the next time you are asked to take personal indemnity as security: Is the man who offers it the kind of a man who will make great personal sacrifice to keep his word with you? Is he the kind of a man who wants to pay his moral as well as his legal obligations? Is his word as good as his bond? If it isn't, don't take either his word or his bond.

Now I have said the chances are only equal even if he is able to pay. He may live in affluence and luxury and yet be wholly free from the hands of lawyers, collection departments and courts of law. In addition to all of his chances to escape by hiding his property are the many and varied chances he has to escape through the use of his technical defenses.

Personal indemnity, of course, is personal surety. There isn't one among you, who are solicitors or underwriters of surety bonds, that hasn't at your tongue's end many, many reasons why personal surety isn't good or safe and why it isn't in line with sound principles of business to-day. And yet you are sorely tempted by some fellow who flashes a fake financial statement on you to take his personal indemnity as your only security for an obligation which, when it fails, is absolute as against your company.

ADVERSE PRECEDENTS.

In the transaction of writing a bond and taking personal indem-

nity, the present rules of law and the practices of the courts are against you in two ways:

First—On a claim on the bond they are against you on any technical defense you may have; and the weight of all sentiment is against you even though you have a good defense to the merits of the claim.

Second—On your claim against the indemnitor they are against you and in favor of your indemnitor when you undertake to salvage your loss.

In other words, all the old rules favoring the surety are in full force and effect in favor of your indemnitor, but, as you no doubt know, these rules have been abrogated and are no longer applicable to the paid surety under the decisions in most jurisdictions.

On these points a few instances taken at random from some of the recent court decisions will serve to distinguish the construction as between the indemnitor and the paid surety.

The old rule as to a surety—and this applies now in all force to the personal surety or personal indemnitor—is stated as follows:

Sureties are said to be favorites of the law, and a contract of suretyship must be strictly construed and must not be extended by implication or presumption (Cyc., Vol. 32, p. 72).

A surety may dictate the form and conditions of his proposed liability, and an acceptance binds him only on strict performance of the contract of suretyship (53 Ill. App., 229).

A surety is not to be held beyond the precise terms of his contract. His liability is strictissimi juris and cannot be extended by construction (122 Ill., 308).

It is a well-established principle of law that the contract of a surety is to be strictly construed and he is not to be held responsible beyond the precise terms of his undertaking. His risk is not to be increased or his responsibility extended without his assent (Ills. Sup., 1845).

And worse yet, listen to this one from the Appellate Court of Illinois (18 Ill. App., 74; also same principle in 82 Ill., 511):

"Parol evidence is admissible to show that a surety limited his liability on signing as surety, to that of surety for a co-surety."

These cases arise where a number of persons, at least two or more, sign the same document, apparently all signing as co-sureties for the same principal. The decision lays down the doctrine that parol or oral testimony may be introduced to show that one or more of the signers did not agree to accept the obligation of the principal, but only agreed to accept an obligation as surety for one of the co-sureties.

NOT HIS OBLIGATION.

Of course, this defense would not be available to one who was sued with the others by the obligee, but it is available as between themselves, and always in the mind of the person so signing there is that belief that it isn't really his obligation; and this attitude of mind toward the whole matter is tremendously important and goes back to our first proposition that the security furnished by personal indemnity rests largely upon the essential that the indemnitor is of a character and manner of thought that makes him want to pay an obligation of this kind.

These decisions show how far the courts will go to release a personal surety from his obligation, even though on the written instrument it is absolute, for they said, "Even so, we will consider oral testimony to show what the real relations of the parties signing the instrument are."

"The doctrine that a surety is a favorite of the law and that a claim against him is strictissimi juris, does not apply where the bond or undertaking is executed upon a consideration by a corporation authorized to make such bonds or undertakings for profit. While such corporations may call themselves surety companies, their business is in all essential particulars that of 'insurers.' Their contracts are usually in the terms prescribed by themselves and should be most strongly construed in favor of the obligee."

You will note what a complete turning over this is of the other doctrine. There the courts say, "A surety may dictate the form and conditions of his proposed liability and yet be entitled to be favored in every doubtful question." Here the courts say our contracts must be most strongly construed against us.

One of the victims of a Wallingford scheme is said to have referred to him as "having the law working for him like a trained rat." The same thing may well be said of the personal surety who doesn't want to pay.

DANGER OF PERSONAL SURETIES.

Bitter Experience Best Teacher of the Public—"If thou art become surety for thy neighbor * * * thou art snared with the words of thy mouth."—Proverbs 6-12.

By Collins Graham, Manager Bond Department, O'Brion & Russell, General Agents National Surety, Boston, Mass.

When a man has spent years in a highly technical and fascinating business, in a profession which is a distinct benefit to society, reimbursing as it does those who suffer financial loss, many things are brought home to him with startling clearness. And one grave defect in our present business methods which has impressed me greatly—the dangers that individuals run in signing bonds—has made me eager to do what little I can to inform the public of those dangers and point out the ways to avoid them. And I further add that this article is not written as an advertising propaganda looking for new fields in which to increase the bonding business. The bonding companies would not have me do this. Bitter experience is the most compelling teacher. A large mercantile concern which never bonded its employees, thinking it knew more about the laws of averages than men who have made them a life study, shocked and crippled financially by the defalcation of thousands of dollars by a trusted employee, does not have to be urged twice to take out fidelity bonds; neither does a man who, under the guise of friendship, has been led into signing a dissolve attachment bond to later on be forced to satisfy the judgment himself. The next time the man who has suffered loss will inform his friend(?) that he does not sign bonds, but that bonding companies whose business it is to take risks of this kind do. I place an interrogation point after the word "friend." The man who asks another to sign his bond without adequately securing him is on a par with him who borrows money from his friend without intending to pay it back. He is not a friend; he is a contemptible blackguard, a crook.

But to return to bonding companies, bitter experience on one hand and scientific methods on the other are bringing them a natural and legitimate increase in revenue. There is scarcely any field of endeavor now with which they do not come in contact or upon which their influence is not felt. And I needs must mention them because they are the substitute for personal sureties.

The bonds which we are discussing are not investment bonds from which coupons are cut from time to time until they are redeemed at maturity; they are written agreements under seal wherein one party called the principal and another party called the surety promise to do something for a third party called the obligee. These promises are of different kinds, such as guarantees covering the honesty of persons in position of trust, the erection of buildings in accordance with the contract, the payment of money upon the happening of a certain contingency, or the faithful performance by administrators, trustees, guardians and the like of their duties in the probate courts.

THREE PARTIES TO A BOND.

There are always three parties to a bond: the principal, who makes the promise; the surety, who stands sponsor for him and who makes good if he does not; and the obligee to whom the promise runs, who is the holder of the instrument and the beneficiary under it. To make this plainer, let us take a supposititious case. A comes to B, who is the owner of a building, and offers to lease it at a rental of $1,800 per year. B accepts the offer, but as a condition to his acceptance stipulates that A shall file a bond for $2,000 guaranteeing to pay the rental as it falls due and to conform with all the other terms of the lease. A asks C to go surety for him and if he is willing, A and C are bound to B in the sum of the bond as indemnitors in case of default by A. The obligation is satisfied by (1) A living up to his agreement; or by (2) in case of default A or C making good to B the actual damage caused by the default not exceeding $2,000. Demand is made first upon A. If he cannot or does not make good, demand is then made upon C and if he can he must pay. C has recourse upon A for reimbursement if there is any. Experience, though, has shown that very, very often A has not the resources to make good his promise and that the burden falls on C, his surety; also that C, the surety, is unable to satisfy the bond for the reason that he too is financially irresponsible. When both are in this state the security behind the bond is nil and the bond itself therefore worthless. The holder of such an instrument might have saved himself much disappointment, time and trouble if he had not bothered himself about requiring one at the outset.

A worthless bond is certainly an injustice to the holder and an investigation of the reasons for its acceptance by him would more often than not show downright misrepresentation and deception by the persons submitting it and vouching for its worth; and just as certainly does it hurt the moral and business standing of the signer and his surety in the eyes of all who

know the facts. Either or both are liars actually or by implication in leading the holder to believe the bond good when it was of no value whatever; if not liars they are both lightweights in not being willing or able to make good the most formal and binding promise it is possible for men to make. Every surety executive has had enough experience with defaulting principals and irresponsible or dishonest indemnitors to make him a rank pessimist. Personal bonds are bad business for every one concerned as I shall prove shortly. My aim here is to demonstrate that it is just as dangerous to accept a personal bond as it is to sign one, and everything that I say is equally as pertinent to one as to the other.

THE OLDEST INSTITUTION.

Historically suretyship is one of the oldest institutions of the human race. The Bible has pointed out that personal suretyship was practised, was unsatisfactory, and warned against it.

Genesis 43-9: "I will be surety for him; of my hand shalt thou require him; if I bring him not unto thee and set him before thee then let me bear the blame forever."

Proverbs 6-12: "My son, if thou art become surety for thy neighbor; if thou hast struck hands for a stranger, thou art snared with the words of thy mouth."

Proverbs 11-15: "He that is surety for a stranger shall smart for it and he that hateth suretysnip is sure."

And centuries later it was made the theme of Shakespeare's great drama, "The Merchant of Venice."

My purpose is to prove: that there are grave defects in the use of personal suretyship; that there are great dangers caused by these defects; that corporate suretyship does away with all these dangers; and that corporate suretyship is the logical and only substitute for personal suretyship.

Personal suretyship is unsatisfactory for two reasons: because those who become personal sureties seldom receive any compensation for their services and always believe there is no risk, yet nevertheless are often compelled to answer for a default of their principals; and, on the other hand, because such sureties are often found in the case of irresponsible principals to be themselves irresponsible or insolvent, so that real protection is not afforded to those who are entitled to it.

The man who signs a personal bond (the surety) in the first place seldom knows what he is signing or realizes the nature of the obligation which he is assuming. His friend(?) assures him the bond is simply a matter of form, that there is no liability of any kind, and that his signature is an accommodation of the

of any kind and that his signature is an accommodation of the most ordinary character, which he would be glad to return at any time. The signer is not told that he is doing the equivalent of endorsing a note of indefinite term when he signs a dissolve attachment bond. He is not told that his promise is non-cancellable, that he must see the suit through to a final settlement if it takes six years. He does not know that his promise is absolute and unconditional and that even though his principal has the money to pay a final judgment and will not, the holder can demand that he pay it immediately without waiting to sue the former; and not realizing the extent of his obligation, does not stop to reflect that his principal's financial condition could well change for the worse over a period of years, making it unwise to guarantee by him the payment of a sum of money. If he had reflected, how much mental anguish and physical suffering would he have avoided. I could list a formidable number of reasons why a man should not sign personal bonds: such as creating a lien on his property, making it unsalable until the bond is cancelled; becoming involved in litigation and losses, etc., but I wish to go on to those that are the most important, in my opinion.

Those pointed out appeal solely to a man's selfish side, his material welfare. He should not offer a personal bond because it is against his self-interest to do so. The chief reasons, I believe, have their root in ethical grounds—in our duty to give our best to our fellow-men. When a bond with personal surety is offered to guarantee the performance of some act or duty, the holder (whose interest, please remember, is the most important interest) must accept a document the sponsor for which may not be able to indemnify him in case of loss, or if able will probably not be so inclined. The surety company is, in the first place, always able to indemnify the holder of its bond and, second, is always willing to immediately do so upon proof of loss or even formal claim. It must do this to live. The surety company's reputation for making fair adjustments of losses is just as important as the necessity of its being able to pay them. Otherwise it would be discredited. A company that guarantees the honesty of others must be honest itself.

PREFERENTIAL REASONS.

A man of the high type, therefore, would prefer to offer a corporate surety bond rather than a personal bond—

(1) Because he is under obligation to no one for his bondsman. The surety company charges for its services.

(2) Because a personal bond purports to be one thing (good) while it actually is or may be something else (no good) and he would wish to do to others as he would like to be done by—

give the best bond that he could and get nothing less than the best bond in return.

Such a man is true to the principles of corporate suretyship, for the surety business was built and is conducted on honor. The millions, yes hundreds of millions, of dollars of securities under the joint control of our great American surety companies as surety on the bonds of administrators, executors, guardians and trustees are considered as a sacred trust held for the benefit of widows and orphans whose all depends on their estate being safely administered and at the proper time turned over to them. The companies have no financial interest in these securities; it is not in their province to say what they shall and shall not be excepting that they come within the requirements of probate court fiduciaries. But they do say that the principal on their bond shall do his duty, shall administer his trust according to law, and at the proper time turn over to those entitled to them the funds remaining in his hands. Those who are familiar with our business know that when a surety company signs a probate bond it is an absolute guarantee that every heir will receive his rightful due. This is a rule with no exceptions.

Now for the third party—the holder of the bond. The man accepting the security (the obligee) is not effectively protected because the personal surety may die or become insolvent. He usually cannot investigate the finances and standing of the personal surety nor assure himself that the latter has good title to the property which may be offered as the security behind the bond. This inability to verify the worth of the security offered is the weakest of the weak points of personal suretyship from the standpoint of the third party. If one is certain that he has adequate protection, he can by diligence follow his indemnitor's financial condition in a general way, perhaps, and in case of death file due notice of liability against the deceased's estate. But two men can be the closest of social friends and yet know nothing definite about each other's financial responsibility, whether it be strong or weak. A request to sign a bond for the other, or to take a bond with the other as sponsor for the principal, is indeed a delicate matter leading to distressing consequences if refusal is made. Many a man's prudence would prompt him to make sure of his position in a matter concerning the payment of a sum of money, yet rather than offend his friend by openly doubting his word or ability to pay and disrupt a long-standing friendship, he stifles his business instinct, gives in, signs or accepts the bond to most bitterly regret his action later.

POTENTIAL DANGERS.

These are some of the actual dangers arising from personal suretyship. Besides these there is one that is always present—

a never-ending potential danger—the likelihood that your personal surety if called upon will fight before he pays. Thousands of holders of personal bonds, the loss sheets of every surety company, bear indubitable witness that personal sureties never willingly pay. Absolute disregard for their written promise followed by backing and filling and years of litigation in strenuous efforts to avoid liability is the almost invariable rule. Too generally the case is that when final judgments are secured against these sureties no property is found in their hands on which to levy. Transfers to other persons leave them immune or ready for the bankruptcy court. In the occasional case where a man steps up like a man and takes his medicine we find him and his family and business crippled to a greater or lesser degree or even ruined. We sympathize most keenly with each unfortunate individual bondsman. We know beforehand what he will bitterly assert. That he was assured there was no liability; that the bond was only a matter of form and that the principal would of course make good first should that impossible thing, a claim, come in; that he would not have dreamed of assuming such a liability; that he could not afford to take risks like that and besides he was not paid a cent for his services—they were given gratis as a favor to a friend.

This is an old story to us. We are sorry, but our sympathy must go first to the holder of the bond, not to the surety. The bondsman may have been duped into signing, but the holder of the bond, if the principal or the bondsman can make good, will be defrauded if they do not pay.

The interest for whose benefit and protection the bond is given is the paramount interest. A good reason for requiring it is presupposed, else it would not have been given. A bond is not usually offered except it be to the interest of the offerer to bind an advantageous bargain; ordinarily it is required by the party of the second part to the transaction as an earnest of good faith on the part of the party of the first part. The principal and the surety know—if not, it is their duty to know—the nature of the joint and several promise which they bind themselves in the most conclusive and formal manner to fulfill. The holder relies on this security and acts accordingly. Incalculable harm and injury would be done him and thousands of others if promises of this kind were not binding and not enforced by the courts. Many bonds are nothing more than an extension of credit to the promisor. The whole fabric of business is founded on mutual trust and in reliance upon the fulfillment of promises and it is necessary that everything be done which will for the benefit of us all keep a premium on credit instead of substituting a discount in its place. Otherwise the law of contracts, and in fact all law itself, would be cut to the

very roots. Though hardship must fall upon one of two innocent parties, the unsuspecting surety or the trusting holder, justice rightly decrees that it must fall upon the bondsman. Ignorance of the law cannot excuse him.

SURE DISASTER.

It is possible for some people through good fortune or excellent judgment to sign and accept personal bonds freely, but those persons are few and far between. As a general statement it is as safe to say that a continued and reckless signing of personal bonds will lead to disaster just as surely as the same procedure in endorsing or accepting notes or a course in reckless dissipation will end in trouble. It simply cannot be otherwise. The companies transacting suretyship in the United States in 1915 paid out in cash over $7,291,000 on losses and claim expense. Think of that for a minute. And these seven millions of dollars represent a most carefully selected class of risks. If there is any one thing that should bring home to the public the dangers in signing bonds it is this exhibit of the loss experience of our great companies. These losses occurred from obligations it was considered safe to assume after years of experience and organization and with knowledge of the many features of the risk involved. How, then, can the unwary layman hope to blunder into anything except trouble?

There is nothing that can bring home more forcibly to people the folly of any course than the relating of actual cases. As fair examples bringing out the dangers I have mentioned I will quote at length from an article which appeared several years ago in the *Insurance Post* of Chicago on the well-known Laing case, which needs no comment from me. Then from Illinois I will take you to Massachusetts and show you what a disastrous experience the city of Newburyport had with personal sureties; from there to the State of New York.

"The most conspicuous recent instance in Illinois is the Laing case, in which judgments for $245,000 were rendered against personal bondsmen, which had to be paid to the extent of their ability, although they had taken every precaution to protect themselves against liability. In 1888 Cuthbert W. Laing was appointed guardian of the estate of his minor daughter, then twelve years of age, Laing having barred himself from any participation in his wife's estate by an ante-nuptial agreement. He gave a guardian's bond of $65,000, with Herbert A. Streeter, Benjamin F. McNeil and W. A. McNeil as sureties. Laing dissipated the estate and suit was begun in the Circuit Court of Cook County against Laing and the bondsmen, the case being finally decided in June, 1908. A judgment was given before Judge Pinckney in favor of Mrs. Malcolm, Laing's daughter, for $78,406, and a

creditor's bill was filed upon the judgment. The property of the bondsmen was taken over by a receiver and the judgment was finally compromised, H. A. Streeter paying $13,000 in cash and turning over $17,000 worth of property, in addition to defraying the expenses of the suit, which were considerable. Streeter was eighty years old, and the compromise was made in order that he and his wife might end their years in peace instead of being compelled to fight long litigation. Service could not be had on the McNeils, while Laing himself was insolvent.

A CASE IN POINT.

"There was another interesting angle of the Laing case, equally emphatic in its lesson as to the dangers of personal suretyship. In 1892 Laing, as guardian, filed a petition in the Probate Court of Cook County asking permission to sell certain real estate belonging to his daughter, which now forms part of the site of the Marshall Field building. Permission was granted on the filing of a bond of $200,000, which was furnished by Laing, Vincent C. Price and William E. Mason. Dr. Price is the well-known baking powder man and was then president of a Chicago bank. He signed the bond on condition that Laing would deposit the proceeds of the sale in his bank. William E. Mason, who afterward became United States Senator from Illinois, was attorney for Laing. Miss Laing came of age in May, 1894, and in 1902 married a Mr. Malcolm of Ann Arbor, then for the first time learning that she had any estate of her own, her father having always represented that their interests were joint. In the fall of 1903 Mrs. Malcolm retained counsel to recover her estate, the hearing in the Probate Court showing that Guardian Laing had mismanaged the property and failed to file reports, and that the bondsmen had taken no steps to require him to perform his duties properly. After a prolonged hearing the Probate Court rejected the accounts filed by Laing and found him in arrears, after allowing credit for all the properties in his hands, in the sum of $248,000, of which $88,000 was due under his general duties as guardian, and the balance as proceeds from the sale of the real estate covered by the special bond of $200,000. In the meantime Price had secured from the daughter a release discharging him from all liability as surety, but this was set aside by the court as void on the ground of fraud, and a decree was entered against Laing, Price and Mason for $166,000. No property could be found belonging to Laing or Mason, and the judgment was finally settled by Dr. Price paying $100,000 to Mrs. Malcolm."

The following clipping appeared in the Boston *Post* on January 5, 1917:

BONDSMEN PAY IN ONLY $1550

Felker Defaulted in Sum of $86,000

NEWBURYPORT, Jan. 4.—A settlement has been made with the bondsmen of James V. Felker, who defaulted in 1906 in the sum of $86,000 while city treasurer. The matter has been pending ever since that time, and there have been several overtures made by the past city governments to clean the matter up.

All that appears on the city treasurer's books as having been paid in settlement is $1,550, three of the bondsmen paying $500 each and one estate paying $50. Others have been deemed too poor to pay and in other cases there was some question as to liability on technical grounds. Still others were deceased, leaving no assets to pay any liability.

In all there were 16 bondsmen on different bonds, which represented $80,000, and which the court held were liable for all the years in which the defalcation was shown.

These cases went to the Massachusetts Supreme Judicial Court five times and once to the United States Supreme Court.

James V. Felker was first elected treasurer and collector of taxes of the city of Newburyport in 1883, and after having served in office continuously for twenty-three years, was removed in 1906 upon the discovery that he had embezzled over $86,000 of the city's money, was convicted and sentenced to a term in the State prison. He filed his first official bond guaranteeing the faithful performance of his duties in 1894. It was renewed in

1898, again in 1900 and again 1901, a new instrument being executed each time. Ten sureties bound themselves to the amount of $2,000 each, making the penal sum of each obligation $20,000. No statements of the financial condition of the sureties were required by the city or any steps taken to satisfy the city officials that the sureties were financially responsible. It developed later that some were not. There was a substitution of personal sureties from time to time so that the city had sixteen different men to proceed against in recovery for its loss, these sixteen signatures representing a total liability of $80,000, nearly the amount of Felker's thefts. The city sued several of these bondsmen and won the test case that governed all the others (Newburyport vs. Davis, 209 Mass., 126, decided in 1911), judgment being issued for the full penal sum of each bond, execution for the net loss to the city by the defalcations occurring during the period covered by each bond. Of these sixteen bondsmen, one went into bankruptcy, another made an assignment, another put a mortgage upon his real estate and concealed the proceeds, and still another conveyed his real estate before any attachment could be made, so that of the total number only eight made payments and these altogether amounted but to $13,432.

SAVING THE BONDSMEN.

The principal efforts of the city, through its special counsel, were directed to recover as much as the city could to reduce the amount of the embezzlement, and to save so far as it could the bondsmen from personal loss, owing to the large number of bondsmen and the prominence of many of them—an effort in which they did not co-operate and of which they were largely unappreciative. After all the cases which the city brought to recover back money had been settled, in some of which it was successful and others in which it was not, there still remained a large amount and this was settled by votes of compromise, and finally all of the bond cases were disposed of by compromise and the matter is now closed, after many years and after enormous expense to the city.

Felker began stealing by investing in wildcats, and probably started very slowly to use the city's money. For a time this was easily concealed, owing to the lax methods of auditing his books and personal confidence which everybody had in him, but finally the amount became so large that it had to be covered up and this was done by making city notes, on which he obtained the signature of the mayor by the simple representation that they were renewals of some note of the city coming due. He would sell these notes and deposit the proceeds to the account of the city. It was necessary for him to pay many of his obligations by check, and for this purpose he used city checks.

He so arranged matters on many of these checks that he could show on his cash where he had covered many of them with his own funds, and auditing officials did not deem it necessary to stop him from using city checks to pay his personal bills, although they must have been cognizant of it. In endeavoring to lessen the loss the city brought numerous suits against people who had received checks of the city in payment of personal accounts, many of whom had received Felker's checks in entire ignorance that there was any liability in accepting the city's checks. These had to pay back, and in many cases it was a real hardship because the individuals had sold such things as the necessities of life and in entire ignorance of his misdoing. Much larger amounts were recovered from purchasers of the notes, owing to circumstances under which the notes were issued, but some of the noteholders successfully defended these cases, owing to technical rules of law.

An important point is that the city of Newburyport would have been saved a very large amount of money spent in litigation if it had required a surety company bond, because in that case it would have called upon the surety company for the penal sum of the bond and let the surety company be subrogated to its rights in recovering from persons who had received notes or checks of the city of Newburyport, and technically chargeable with knowledge of illegality in their issue, but this case being personal sureties, and endeavoring to save them from loss and realizing also that the loss exceeded the possible recoveries upon the bonds, efforts were made to make it as small as possible. This case brought home to the people of that city the imprudence of signing bonds, and also to the city officials the wisdom of requiring corporate surety bonds, thereby saving themselves from any compunctions, prompted by sympathy, in enforcing their bonds to the fullest extent.

TWENTY-SIX GRANDCHILDREN.

About 1878 in one of our Eastern States (New York) a widely known country doctor died leaving an estate of $65,000. He, cutting off his seven living children without a cent, left his estate in trust for the benefit of his grandchildren, the income to be paid them annually in equal parts until the youngest child of the youngest grandchild became of age. There were ultimately twenty-eight of these grandchildren, and if his instructions had been carried out the trust would have been in force to-day—nearly forty years after his demise. He nominated as executors to succeed themselves as trustees two friends, one a business man of good standing, the other the cashier of a State bank, the president and owner of which was reputed to be a millionaire. The will exempted them from furnishing official

bonds as such, which was the first mistake. Seven years passed without any shadow of trouble, the estate having been settled and all the assets turned over to the trusteeship. In 1885 the business friend died and here occurred mistake No. 2. The will stipulated that the surviving trustees should continue on alone instead of requesting that the court appoint a successor in event of death. It would have been better if the will had not stated anything about death or succession. Most of our States have statutes designed to cover this very contingency, at the same time making provision for the protection of the heirs' interest by means of bonds, and if this doctor had not, fatally as it turned out, inserted this provision, the court would have appointed a successor to the deceased trustee requiring him in the absence of the assent of all the heirs to file an official bond with sureties. This might have helped a little in the wreck that followed. The doctor cannot, though, be censured for not specifying that his fiduciary should furnish a corporate bond for his was the day before surety companies. The first one transacting the lines now developed was organized and started operations in 1884 and it was not until the early nineties that the advantages of corporate suretyship became known and the business assumed large proportions.

Well, another period of years passed with the bank cashier in full charge. It seems almost unbelievable to state, yet not one of those twenty-eight heirs had the interest, business acumen, judgment or what you will to see that the man who had the handling and control of their money made a verified accounting of his trust; yet they never even broached the subject to him. And perforce they were mightily astounded when ten years after the death of the co-trustee and seventeen years after the demise of their grandfather the cashier absconded after having embezzled and sunk in profitless enterprises many thousand dollars of the bank's funds and all of their estate.

EITHER BOND OR TRUST.

The unrestricted control of other people's money without the necessity of accounting for it undid this man. As long as the other trustees was alive to watch his operations his acts were above criticism; but when all checks were removed he became drunk with a recklessness probably engendered by a contempt for the assinine stupidity of these heirs. If they did not care what he did with their money, certainly he did not. He knew that it is a difficult thing to put a man in jail for mismanagement and harder to get any property from him if he takes pains not to have any; so, careless of his reputation and regardless of consequences, he squandered the entire estate, so much so that when the crash came no salvage was ever recovered.

If you have an estate and you wish to be able to die confident

that it will reach those for whom it is intended, make a will, by all means. But if you leave its handling to an individual, do not exempt him as your executor or trustee from filing an official bond. Stipulate rather that he shall furnish a bond equal in sum to the amount of the estate, executed by some reputable bonding company as surety. Either that or nominate a trust company to perform the duties. Then you can rest assured that each and every beneficiary will receive his rightful due. A surety company on the bond or a trust company giving its own bond is an absolute guarantee of security with no exception to the rule. If you do this no stain of carelessness or poor judgment or failure to have properly acted for your family can then be registered against your name after you are gone. You owe it as a duty to yourself to be prudent and far-seeing. What sense is the sacrifice of a lifetime or the good of years of saving, the payment of many life insurance premiums, or the accumulation of real estate, if you do not place the very best safeguards you know to protect them when you are no longer here to direct the management of your affairs? You count as of little moment a lifetime of effort if you do not.

If you are an heir, ordinary business acumen should prompt you to see that your interests are protected. 'When you are left an estate, that estate, subject to the claims of creditors, is yours, and the fiduciary appointed by the court is appointed to serve the creditors and *you*. He is accountable to you if he fails to properly perform his duties, and any bond that is filed is filed to protect creditors and *you*. Therefore any demand of yours to file accounts, to check over and verify the assets, to furnish an official bond, is a perfectly proper one with which he can be *compelled* to comply. He is receiving a remuneration for his time and services so that he can raise no valid objection to any request of this sort. If, however, you do not feel like "keeping after him" you can safely waive everything except the bond. If you force him to furnish a corporate surety bond you are perfectly safe, as the surety company then assumes the responsibility of doing all which you otherwise ought to have done in that connection, and if it is remiss or negligent in seeing that your fiduciary conforms with all the rules of probate practice, then it has to pay and pays *you*. Their premium is the fee for assuming the risk and their confidence in assuming it lies in their experience and organization.

Surety companies are in an infinitely better position to assume the risk that something will be done than an individual can possibly be. They not only expect to have a certain percentage of their principles default, they *know* they will and that losses will accrue just as surely as they charge a premium for their services. The individual, on the other hand, as previously

pointed out, never expects to be called upon; if he had had the slightest doubt he would never have assumed the responsibility. The surety companies are ready and willing to pay their just losses promptly; the individual is always unready and always unwilling. The surety companies operate under rigorous State supervision and their financial condition is at regular intervals carefully examined by the State insurance departments. They must set aside by law a certain percentage of their premium income as a reserve against future claims. Limits are imposed by the Government as to the liability which they may assume on any one bond and tables governing these limits, showing their capital and surplus, are published quarterly by the Treasury Deparment. The individual not only fails to set aside a reserve to protect the holder of his bond in case of claim but also fails to make adequate provision for loss to himself.

THE TEST OF SERVICE.

Finally, there is the test of service. Corporate suretyship has come through every test of better service, surer protection and prompter payment in case of default. A number of our cities and courts now specify their preference for corporate surety and everywhere it is accepted. If individual sureties could find out from their principals the real hazard and definitely know what they were doing before they became sureties, and if holders of personal bonds were adequately protected by the sureties, the argument for corporate suretyship would be less strong; but the impossibility of so doing has theretofore been shown. Therefore corporate suretyship is the logical substitute, the only substitute, the better practice, the surety of the future.

Such being the case corporate suretyship should be universally used. And why is it not used everywhere? Simply because of ignorance. The people do not know about bonds or the dangers that surround them. I venture to say that millions in this country have never been called upon to furnish one; therefore they either do not know what manner of things they are, or, having heard of them, have the haziest of ideas and confuse them with investment bonds. And if they are ignorant of the bonds themselves they naturally cannot be in a position to judge the hazard or place the liability that accompanies the signing or accepting of any of them. I am informed that more than half the small towns in the State of New York still cling to personal sureties on the official bonds of their town officers. This is hard to believe of the greatest State in the Union, yet is undoubtedly true. And these towns will continue to cling to personal suretyship until the march of progress reaches them and they make the change of their own accord,

or until they or some neighboring town are hit hard and learn the lesson by bitter experience. Outside of the bonds filed in the probate courts guaranteeing the handling and settling of estates, no greater good can be done by surety companies for society than endeavoring to reach these towns, for the situation in New York is true to a greater or lesser degree in all the other States, and bring home the dangers of personal suretyship and the vital necessity of abandoning it. Thousands upon thousands of dollars will be saved taxpayers from making up losses on irresponsible personal sureties; a higher grade of public officials will be selected to meet the surety companies' underwriting requirements; modern business accounting methods in place of the present lax ones will be installed in town offices, and town officers will be made independent of obligations to politicians.

PEOPLE MUST BE TOLD.

The pressing question to be solved is *how* to educate the people, for education is the only way. People will never know about the advantages of better methods until they are told about them. Our great mission, then, is to find out the best method, and then, like true missionaries, to put our hearts and heads and hands to the mighty task that lies before us. And the general public are not the only ones who are in the dark. It is a matter of continual comment among surety men in our State why it is that Massachusetts probate judges will require a bond of $1,500 where the estate amounts to $1,000, but will order a bond of only $100,000 where the estate amounts to $500,000. The logic of this is difficult indeed to follow. Perhaps they think a person can more afford to lose a large estate than a small one. Neither is the reasoning clear why Lawrence, a city of 85,000 people, requires its city treasurer and collector of taxes, a dual position—one man filling both—to file a $50,000 bond when over $1,500,000 pass through his hands each year. A $50,000 bond is a farce; it should be 5 times that amount, at least, and much greater than the sum which he might have in his hands at any one time. The trouble is that more regard has been given to the person filling the bond than to the one to whom it is given. Equity and justice demand the reverse, and bonding companies were evolved that fair play might exist.

WHAT A JUDGE THINKS.

As instances where the judges of probate regard the situation in its true light, I quote from the *Ætna-izer,* the Ætna Casualty and Surety Company's monthly journal, issue of December, 1916:

"SUPERIOR VALUE OF CORPORATE SURETY BONDS."

"A lawyer was bonded by a corporate surety company as

the guardian of 2 young boys, whose father had just died. After a time the lawyer disappeared and it was found that he had left a shortage of about $8,000 which was within $100 of the amount of the bond which the bonding company promptly paid.

"The matter came before Judge Stewart Hanley of the Wayne Probate Court at Detroit and evoked from him the following comment:

"'If that had been a personal bond you can see what the results would have been. Bonding companies invariably are prompt about settling up while if an individual is on a bond, it is only natural that he should fight liability.'

"'If the same high quality of bonds were asked in the criminal courts as are asked in the probate court, there would not be any trouble about making collections on forfeited bonds, such as the county has experienced recently.'"

Surrogate Fowler of New York County, in a recent decision, said in part as follows:

"Forty-six per cent of the guardians named without bonds under the new law are in default. If we were to call them to account, having given no security. they would not respond to the decree, and to commit them to the common jail for disobedience would be a great public charge. These helpless children thus defrauded are now beginning to complain aloud to this court, but their cries, to my sorrow and regret, must this time fall on a deaf ear, as where no bonds have been required of the guardians, they are, in every instance, personally irresponsible."

It is men like these and happenings like these that will make corporate suretyship not only the surety of the future but the universal surety of to-day.

PERSONAL SURETYSHIP FOR STRANGERS.

Too Much Reliance on the Principal's Statements—Exhaustive Investigation Necessary.

By H. E. McClellan, Chief Auditor of the Maryland Casualty Co., in the Fidelity Journal

It seems strange that any one who is asked to sign the bond of a public official whom he does not know, would sign that bond without investigating the man. Certainly he would not do that in his individual and personal capacity. Why, then, is it so frequently done by the same person who, instead of acting in his personal capacity, is representing a surety company? And yet that is exactly what seems to be done day in and day out.

There is no intention to imply in the foregoing that all agents will sign bonds without being careful to inquire into the ability, standing and general reputation of the official in question, but we repeatedly receive papers in connection with executed bonds which convey absolutely no information whatever about the principal beyond that given by the principal's replies in his application; cases where our subsequent investigation brings us unfavorable information so definite and conclusive, information which is so generally known and thus so easily obtained, that by no stretch of the imagination could we figure that the agent who executed the bond made any serious attempt to inquire into the qualifications and standing of the man on whose behalf that bond was written.

The opinion which many agents seem to have regarding public official risks is that if a man is unfitted for the position, or is not what he should be, he would not be elected or appointed. That of course is all bosh. because as a matter of fact there is perhaps no business under the sun where more undesirable, unreliable and incompetent characters are taken care of than in public offices. Therefore, instead of assuming that a man is a desirable risk because he has been given a public office, that very fact should prompt the agent to make a most exhaustive investigation before exercising the authority vested in him under his power of attorney, and if the risk is one of a class or in a penalty which he cannot execute under his power, then the application should be transmitted to the home office, together with the report setting forth the result of the investigation.

Another opinion held by many agents is that unless the official handles a great deal of money there is no liability under the

bond. To use their favorite expression, "The bond is a mere matter of form." As a matter of fact, there are a great many bonds where the officials handle no money but where the surety's risk is nevertheless proportionately greater than where the official handles funds. Sometimes the risk is many times more hazardous than the risk on a treasurer, for instance, because suits for damages resulting from the failure of an official to do those things which the law requires him to do, or because he did something he should not do, are exceedingly uncertain, not only in the matter of possible recovery, but the amount of recovery as well, and in addition to this the surety is always confronted with the possibility that the cause resulting in the suit may not come to light for years, perhaps even long after the death of the principal. In other words, defalcations, as a general thing, are fairly promptly discovered, but suit for damages may be brought and recovery made years after and the official has been forgotten. We cannot emphasize too strongly the absolute necessity of an exhaustive investigation in order to determine positively whether the official possesses the ability and all the qualifications necessary for the performance of the duties and responsibilities of the office to which he is elected or appointed, and whether he is conscientious and careful in the performance of his duties and honest and honorable.

When an agent is given power to assume liability for the company, it is given with the firm belief that the agent will be as careful in exercising that power and looking after the interests of the company as he would be in transacting his personal affairs. If we cannot count upon him to that extent, or should we find that the degree of care he gives to his personal business as well as ours is less than good business judgment and prudence make necessary, then we certainly cannot permit him to execute any bonds after we have learned of that fact. Signing bonds is not an incidental something. It represents the assumption of liability in every case and we are not willing to assume that liability ourselves or have the agents cause us to assume it for any person unless everything tends to show that that person is entitled to the degree of confidence and to the extent of credit represented by the bond he is applying for.

JOINT CONTROL OF ASSETS.

Prevents Appropriation—Secures Performance of Duty by Principal—Requires Much Knowledge and Care from Company.

By Luther E. Mackall, Assistant General Manager of the National Surety, Author of "The Principles of Surety Underwriting."

In Volume One of Live Articles on Suretyship (page 54) there is a discussion of the subject of joint control by a surety company of the assets in the hands of a fiduciary bonded by it. The importance of obtaining joint control was pointed out and some suggestions were made as to reasons or arguments that might be used in persuading applicants to give the surety company joint control.

There is, however, another angle to the matter of joint control. Joint control is desirable because—

(1) It may be the means of preventing the principal from appropriating any part of the estate to his own use, and

(2) The surety company may thus be able to see to it that the principal properly performs his duties and that he disburses the assets only for proper purposes—purposes which are authorized by law and which the court having jurisdiction has approved or is legally bound to approve. The latter feature is important because the surety on the bond of an executor, administrator, guardian, trustee, receiver or other fiduciary is liable not only for actual thefts or wilful misappropriations by the principal, but also for any loss resulting from any failure to perform his duty even though the error be committed in good faith. The exercising of joint control is therefore not a merely perfunctory matter of countersigning checks. It requires considerable knowledge and care on the part of the surety's representative, as shown by the fact that the surety companies each year sustain considerable losses through the fact that their agents permit money, of which they have joint control, to be improperly withdrawn and expended.

It is impossible in the space permitted for this article to show precisely when it is proper to permit funds to be withdrawn and when it is not proper. Even if it were possible to do so, that would involve a full statement of the duties and liabilities of the fiduciaries and a full statement of the circumstances under which disbursements may properly be made. It will be possible

only to indicate a few of the cardinal rules which should govern the agent charged with the duty of exercising joint control.

SECURE ORDER TO GIVE JOINT CONTROL.

1. Having obtained the promise of the applicant to give joint control and having executed the bond on that basis, the first step is to have him sign written directions to the custodians of the assets to permit withdrawal only with the consent of the agent. Forms are usually provided by the companies and one of these forms should be filled up and signed by the applicant and served upon each bank in which any money belonging to the estate is deposited and with the safe deposit company owning the vault in which the box containing the securities, if any, is located. This will operate to prevent the withdrawal of any of the cash or securities in the hands of those particular custodians.

GET ALL ASSETS UNDER JOINT CONTROL.

2. The agent should see to it that all the liquid assets are under his joint control. He should check up the assets under his control with those shown in the application, and he should verify as far as possible that those are all of the assets. He should see that a sworn inventory is filed promptly and should obtain a copy and check it against the assets under his control. The first duty of a fiduciary is to secure possession of the trust property, and the agent should see that this is done and that the property is put under joint control. If there are debts outstanding, these should be promptly collected and the proceeds put in the joint control account.

IDENTIFICATION OF THE ASSETS AS TRUST PROPERTY.

3. It is important that the funds and property of the estate be identified as trust property. To this end the bank account should be kept in the name of the estate or in the name of the fiduciary and followed by such language as to show that the money belongs to the estate; as, for example, "John Smith, Trustee under the will of Henry Jones." Likewise, the safe deposit box should be rented in the name of the estate and in the name of the fiduciary, in his trust capacity. The securities belonging to the estate should, if possible, be placed in the name of the estate, so that they cannot be transferred except upon the signature of the fiduciary.

The importance of the separation and identification of the trust property ought not to be underestimated by the agent. If, for example, the bank account is carried in the individual name of the principal and the bank should fail, he and his surety would be liable for the resulting loss, even though care had been used in the selection of the depository, while if the

account had been carried in the name of the estate, the fiduciary and his surety would not be liable. There are other possible complications which make the separation and identification of the trust property important.

ASSETS SHOULD BE WITHDRAWN ONLY FOR PROPER PURPOSES.

4. Having gotten the entire liquid assets under joint control, the agent must then be careful not to permit any of it to be disbursed except for proper purposes. If the estate is liable for the payment of debts, as is always the case of the estates of deceased persons and of bankrupt and insolvent estates, it is the duty of the fiduciary promptly to give notice by publication, in the manner provided by law, of his appointment, to the end that all who have claims against the estate may have an opportunity to present them. As a rule, no debts should be paid until after the expiration of the time within which claims may be filed, for if some should be paid in full and subsequent claims should make the estate insolvent, so that the creditors would not be entitled to full payment, there would be an overpayment for which the fiduciary would be liable. Generally, however, there is no objection to paying individual items which have a clear priority, such, for example, as taxes, and in the case of estates of deceased persons, the funeral expenses of the deceased. After the expiration of the time for filing claims, and if there is enough money in the estate to pay all claims, it is proper to pay such of them as have been allowed by the court, retaining on hand enough to pay any that may be disputed.

INVESTMENT OF FUNDS.

5. In the case of executors, administrators, receivers, assignees and other so-called short-term trusts, the fiduciary is not expected to invest the assets, but simply to convert into cash such of them as it is necessary to convert and to distribute them to those legally entitled thereto. In the case of guardians of minors, conservators of incompetents, trustees and other so-called long-term trusts, the fiduciary is expected to keep the assets properly invested so that they will yield an income without affecting the safety of the principal. The question what is and what is not a proper investment is a difficult and complicated one and depends upon the law in the particular State. The main point which the agent should bear in mind is that the money of the estate should be invested only in first-class investments, such as are commonly called "gilt edge." The New York rule, which is in force not only in New York State, but in a number of other States, is that trust funds ought to be invested only in government, State or municipal bonds, first-mortgage bonds of corporations and first mortgages on real estate. Other States, including Massachusetts, have a somewhat more liberal rule, but

the New York rule is the conservative one and should generally be followed. A fiduciary gains nothing by making doubtful investments, for he must account for all profits and is responsible for all losses; and his surety has the same responsibility. As a rule, trust funds should not be invested in stocks of business corporation; and of course they should not be invested in loans, personal security, nor any business ventures of any kind, nor in second mortgages or mortgages on leasehold property, nor any investment of an untried or speculative nature.

ACCOUNTING.

6. Each fiduciary should file an account as often as is required by law, generally once a year, though the rule differs in different States. The agent should procure a copy of each account and should check the balance as shown by the account with the balance subject to joint control. If they do not correspond, it is time to make an investigation.

DISTRIBUTION.

7. As a rule an agent should not permit any of the assets to be distributed until a final account has been filed and approved by the court and until the court has issued an order directing how the distribution shall be made. Agents are often asked to permit payment of a sum of money on account to one who claims to be a beneficiary. Such a proceeding should not be allowed by an agent under any circumstances. If the circumstances warrant, the matter may be referred to the home office, but as a rule it involves many dangers for the surety. A fiduciary must not only distribute the estate promptly when distribution is due, but he must at his peril distribute it properly. If he distributes the wrong amount or pays it to the wrong person, he must bear the loss. The fact that he has been diligent or has taken advice will not save him. The best protection is to obtain the decree of distribution. Likewise, the fiduciary must at his peril pay the distributive shares to the identical persons named in the decree or their proper representatives; and the agent should not countersign any checks until he is certain that the distribution is being made to the proper persons. Vouchers or receipts should be obtained and should be filed in court with the papers relating to the estate.

It is hoped that these suggestions will be of some assistance to the agents in the handling of joint control accounts.

CHECK RAISING SURETYSHIP

New Form of Surety Coverage—Two Leading Examples by Prominent Companies—Important Line for Agents.

By E. C. Lunt, Vice President, in Charge of the Bonding Department, Fidelity and Casualty Company of New York.

Business men are constantly buying mechanical devices intended to prevent alteration of the amounts written on their bank checks and drafts. While these "check protectors" vary in value, none affords real protection—a fact sufficiently attested by the ease with which competitive salesmen change a check that has been "protected" by a rival machine. Furthermore, this protection, such as it is, extends only to the amount of the check, and leaves at the mercy of dishonest penmen the date and number of the check as well as the name of the payee. At best, the check protector is a time-consuming nuisance. It does not prepare the entire instrument, and it necessitates two distinct operations in such preparation—a matter of considerable moment to large users of checks.

Under the conditions described the Fidelity and Casualty Company has recently placed on sale agreements to provide real check protection in the form of a policy of insurance against loss from check alteration. This policy relieves the drawer of the check from the burdensome use of any protective device, and provides complete protection (up to the policy limit) against any alteration of the name of the payee or the date, number, or amount of the check. The National Surety also has such a policy.

"F. AND C." CONTRACT.

The Fidelity and Casualty policy reads as follows:

"The Fidelity and Casualty Company of New York (hereinafter called the Company), in consideration of a premium of ......dollars payable annually in advance so long as this policy shall remain in force, does hereby agree that within thirty days after due proof of loss, it will reimburse......of......State of......(hereinafter called the Assured), for the direct loss, not exceeding......dollars in the aggregate, resulting from the felonious alteration of the amount, date, number, or the name of the payee, of any check or draft drawn by the Assured, while this policy is in force, against a deposit account of the Assured in any incorporated bank or incorporated trust company in the United States, excluding Alaska and insular possessions.

The foregoing agreement is subject to the following conditions:

1. Upon the discovery of the alteration of any such check or draft the Assured shall give immediate notice thereof to the Company by wire addressed to its home office in New York City, and upon the same day shall send by registered mail to the Company at the said address the fullest information obtainable at the time, including the original check or draft in connection with which claim is made. This policy shall not apply to any loss that is not discovered within forty-five days from the date of the payment of the check or draft by the bank upon which it was drawn, nor to any loss from the payment of a check more than ninety days after the date thereof.

2. The Assured shall balance each deposit account maintained by him, at least once in every calendar month, and shall compare such balance with the balance shown by a statement obtained from the bank, and shall obtain from the bank, examine, and verify, by actual comparison with the Assured's records, every check and draft paid during the said month.

3. The terms of this policy shall apply only to checks and drafts drawn and signed in ink in the usual customary manner, and signed by those whose signatures the bank has been instructed by the Assured to recognize.

4. This policy shall not apply to any loss, if the Assured, any partner of the Assured if the Assured is a co-partnership, or any executive officer of the Assured if the Assured is a corporation, is concerned with the said loss, either as principal or accessory.

5. Without prejudice to the rights of the Assured as respects anything that may occur during the period that this policy is in force, the Company may at any time terminate its liability hereunder, as to checks and drafts drawn thereafter, by a written notice served on the Assured, or sent by registered mail to the Assured at the adress hereinbefore stated, at least fifteen days prior to the date that the cancellation takes effect. In case of such termination the unearned portion of the premium shall be paid to the Assured, and the Company's check shall be a sufficient tender of such unearned premium.

6. No change or waiver of any of the terms, conditions, or statements of this policy shall be valid unless set forth in an endorsement added hereto and signed by the President, Vice President, Secretary, or one of the Assistant Secretaries of the Company. Neither notice given to nor the knowledge of any agent or other person shall be held to waive any of the terms, conditions, or statements of this policy unless set forth in an endorsement added hereto and signed by one of the said officers of the Company. The insurance granted hereunder may not be assigned unless the consent of the Company to such assignment

is set forth in an endorsement added hereto and signed by one of the said officers of the Company. All sums that from time to time may be paid under this policy shall be accounted in diminution of the insurance hereunder.

In witness whereof," etc.

While the insurance provided by the foregoing policy is subject to certain conditions, it will be noted that these conditions impose upon the assured no obligations inconsistent with good business practice. Every well-conducted concern, for example, makes it a point nowadays to verify or to correct its own books by comparing them with the monthly statement rendered by its bank; and it is surely good practice (for another example) when a check is not presented for payment within ninety days, to stop payment upon it or at least to investigate the cause of the delay.

The charge for check-alteration insurance is five dollars per thousand dollars per annum—a five thousand dollar policy embodying real protection thus costing only half as much as the least imperfect variety of check-protecting devices. Where numerous checks are issued and machines are used the cost of the bond is soon made up in the saving of clerical time.

THE CHECK RAISING MENACE.

Alarming Extent of This Popular Form of Crime—Typical Cases and Characteristic Methods.

By C. E. Wandel, Manager, Check-Alteration Bond Department, The National Surety Company, New York.

Long before Albert E. Bell, nationally "wanted" forger and mail-robber, tricked Philadelphia merchants out of $500,000, fifteen years ago, by filching a mail bag full of business letters from a truck on the railroad station platform, one dark night, raising the checks he found in the envelopes to large amounts, cashing them at local banks, and flitting safely Westward before the altered checks filtered back to their original signers, the crime of *check-altering* was recognized as one of the gravest and most widespread of all menaces against our nation's business.

American business is vitally and essentially dependent on the daily exchange—by mail or messenger, and in the hands of scores of one's own and other people's employees—of thousands of checks drawn on hundreds of banks of deposit.

Any crime or swindle which makes a special study of the various weak points in this method of daily exchange of checks and which preys upon it to the extent of many thousands of dollars annually, seriously affects our entire American system of doing business. This particular crime of check-alteration is also rendered additionally serious to the average American business man or bank depositor because many high courts of the United States have ruled that, when a check has been raised or altered by a dishonest employee or professional crook, the loss must be borne, not by the bank which cashes the check, but by the innocent depositor by whom it has been signed, if the signature itself is genuine.

WAYS THAT ARE DARK.

Scores of cases of check-alteration take place annually in different parts of the country. Albert E. Bell, the swindler above referred to, operated by stealing business men's checks from the mails, choosing those of the *smallest* amounts and getting these certified at the bank in which they were drawn (the cashier being invariably unsuspicious because of the smallness of the sum apparently involved). The swindler would then increase the amounts of the thus certified checks by adding ciphers to the numerals and the word "hundred" to the written amount. In

case the amount had been stamped on the check by a so-called check-protecting machine, he would leave the amount as it was but would efface the payee's name with tartaric acid and substitute the word "bearer" or "cash." Taking the altered but still certified check to a second bank, Bell would deposit it, stating that he wanted to open an account. Next day, before the tampered check had travelled back to the certifying bank, he would draw out a substantial part of his fictitious deposit and move quickly and safely to another city to repeat the swindle.

Bell's, however, is only one of countless methods by which check-raisers throughout the country prey on business men. To understand all the variations of this widely practised fraud, the reader should, perhaps, first consider that those who are continually practising it belong to two widely separated classes.

One class of check-raisers consists of previously respectable employees of business firms (bookkeepers, cashiers, clerks, etc.) who need money badly to meet some private difficulty or personal desire and who succumb to the ease with which the many checks of their employer, which pass daily through their hands, can be altered and cashed. The second class of check-raisers, equally numerous and operating with equal ease, are professional criminals who obtain checks of reputable business men either by mail-thefts or by one of many small and simple commercial subterfuges, and who, after altering these checks, are able to cash them quickly and without difficulty and with almost complete immunity in a score of ready ways.

THE TRUSTED EMPLOYEE.

Check-raisers of the first of these two classes—business employees of honest antecedents who, needing money badly to meet some personal situation, succumb to the tempting ease with which their employer's checks can be raised and cashed—are especially pathetic types. Among them sometimes are boys too young to realize their crime's seriousness; and girls, immature and only partly educated, who have never had money enough to draw checks of their own. Reasons impelling them to this fateful act are often trifling beyond comprehension. An $18-a-week grocery clerk in Chcago recently raised and cashed his employer's checks for more than $1,000—merely to enjoy a brief fling at fashionable hotel life. A youthful New York engineering corporation employee, having innocently "faked" a bookkeeping balance by altering a $100 check, was encouraged by this to embark on a series of deliberate check-raisings, which totalled $3,000, in order to enjoy a few months' dissipation.

Typical of trusted employees who have in recent years become check-raisers are: a New England shoe store clerk who increased his employer's $12 check to $12,000 by merely inserting

the necessary ciphers after the numeral and adding the "hundred" after the "twelve"; a San Francisco elevator company employee who raised two of the corporation's checks for $3.50 and $400 to $5,500 and $1,400 by a few equally simple pen strokes; a 23-year-old telephone girl who ruined her business career by raising one of the company's $1 checks to $50 and spending the proceeds on theatre tickets and candy.

Previously honest business employees who raise and cash their employer's checks are able to operate with obvious ease because they are known and trusted at the employer's bank. But it is a mistake to think that professional criminals have much greater difficulty in victimizing business men. Each check raising swindle has three distinct successive steps: (1) obtaining the check; (2) altering it; (3) cashing it. All three steps are easy for a professional criminal of ordinary intelligence and personality.

The average business man feels that his check is protected by the amount he has written upon it in his own handwriting. He also believes that the bank will be responsible for any tampering.

THE PROFESSIONAL CROOK.

One class of professional check raisers steals checks either from mail pouches, or from private or public letter boxes. One check raiser victimized many New Jersey merchants by getting their mail through opening street letter boxes with a false key. Another swindled Boston and Philadelphia business men by fishing their mail from private letter boxes with a wire.

Small commercial transactions, however, furnish criminals with much easier ways of obtaining checks. A pair of professional criminals cleaned up $300,000 in two years from merchants in American and European cities by starting a succession of small stores, opening bank accounts, raising all checks received for their goods to large amounts, depositing them in their banks, drawing heavily next day against the fictitious deposits and vanishing to repeat the same swindle in another city.

An even more simple method which professional check raisers have employed to obtain checks from respectable merchants is to enter a store, order a large bill of goods sent to a furnished room address, pay cash for the goods, return part of them next day, as not needed, and ask that the refund be sent in the form of a check.

Bank drafts can, of course, be "raised" as easily as checks. Many banks are thus victimized. Professional check raisers bought four $5 drafts from Brooklyn banks, raised them each to $5,000, deposited them in Chicago banks, drew heavily against the fake deposits and disappeared leaving the half dozen banks to a long and complicated law suit as to which would bear the loss.

When professional check raisers fear that a bank will investigate one of their raised checks before allowing money to be drawn out against it, they usually get the check certified at the bank on which it is drawn before raising it. Certification often quiets suspicion of the paying teller who is later asked to cash the check. The average bank official is instinctively more suspicious of being swindled by an uncertified check against which there are "no funds."

Writing on any check can be effaced in five minutes with tartaric acid and chloride of lime. But even the young and inexperienced can raise a check to thousands of dollars with a few unnoticeable pen strokes. Indeed the popular notion that checks can only be raised by specially gifted forgers materially assists the success of this widespread and easy form of crime.

So-called check protecting machines only partly prevent checks from being seriously tampered with. They protect the amount by stamping it into the paper. They do not, however, protect the date, serial number and payer's name. Any check, stamped by a so-called protecting machine, may easily be cashed by effacing the name of the payee and substituting the word "cash" or "bearer."

The only absolute and complete way for a business man to protect himself from loss through the alteration or raising of his checks is to carry a "check alteration bond" under which some reputable surety company agrees to indemnify him in full for any such loss, in exchange for a small fee.

THE VALUE OF A CLEAN RECORD.

The Way of the Bonded Transgressor is Hard—What Corporate Surety Means to Business Men.

By Collins Graham, Manager, Bond Department, O'Brion and Russell, General Agents, National Surety, Boston, Mass.

I know of no sound argument which can be advanced against a clean record; among the innumerable reasons why one should be most highly prized and jealously guarded is the close relation between a clean record and success in business. And by a clean record I mean—a daily life of absolute honesty in money matters, the prompt payment of debts incurred, a total abstinence from gambling, a high standard of morals,—with the resulting fine reputation for integrity and force of character. Of course we do not seriously object to an occasional cigarette or glass of beer if the application shows he can afford it but, jesting aside, a man cannot be too circumspect about his habits and character. His reputation is largely formed from them, and bonding companies agree with Burke that there never was a bad man who had ability for good service.

The enormous growth of our American surety companies in recent years is one justification for their existence; their painstaking stewardship over the hundreds of millions of dollars in their joint custody as surety upon the bonds of administrators, trustees, guardians and the like for dependent widows and children is another; the one which I have in mind, namely, the premium which the requirements of our honesty guarantee bond puts upon a clean record is a third.

To-day the ramifications of our business are practically without limit. Our influence is becoming more widespread and powerful every day, especially in the business world, and it behooves that great army of workers—the money handling employee—to know something of our methods of sizing up his fitness for our bond, *our* standards, and what we expect his standards to be.

We expect every man in the service of a firm or corporation to be honest. What we sometimes get, however, is best illustrated by Willie's answer to his English teacher. She read, "Enoch was loved of God and God took him." "Now, Willie, you may repeat to the class what has just been read." Willie after a somewhat lengthy pause answered, "Enoch was not what God took him for." And so it is with us; some men are not

what we take them for. However, when they are not they are usually sorry, for the way of a bonded transgressor is hard. Surety companies are not soulless nor merciless, but they aim first of all to keep their premium rates down by keeping the losses down, and they need the strong arm of the law to make the consequences of wrongdoing extremely unpleasant if not unbearable. For that reason I am in favor of prosecution in all cases, excepting where there is good cause for leniency.

RECORDS COUNT.

However, the number of losses paid to the number of bonds issued is very, very small, some fraction of 1 per cent. The percentage of losses paid (including claims expense) to net premiums in 1917 ranged from less than 5 per cent. in one instance to over 205 per cent. in another among the American surety companies writing fidelity bonds. The fact that such an enormous loss ratio as indicated by the last figure is *possible* from the comparatively trifling number of defaults out of all the bonds issued shows how careful the surety companies must be. And as no collateral is taken from his to secure us, our decision to issue the guarantee resting entirely upon the applicant's past record and reputation, it naturally follows that his past should be favorable to warrant faith in his future. Employers do not engage or promote men unless their record indicates their fitness for the new position. Surety companies simply cannot afford to guarantee the integrity of money-handling employees unless their record *proves* their past honesty and indicates sufficient strength of character and purpose to withstand under all circumstances the temptation to steal. If our applicant appears to have the qualifications which the position demands and he has a clean record, we (by that I mean all surety companies) will help him to secure that position by issuing our bond, which is the strongest recommendation that a man can secure in the business world to-day.

We believe, we *know,* that the great majority of men are honest. We know that this is true because our business and success have been based upon that premise. Our active American surety companies at the close of 1917 had in force, upon which they were liable in case of default, bonds aggregating $2,845,000,000 upon a net premium income of $10,000,000, and a loss ratio of $2,500,000. It is not to be inferred, however, from these figures that the surety companies are emulating "Get Rich Quick Wallingford." The expense ratio averages 50 per cent. of the premium income, due to the enormous amount of detail work necessary in connection with investigations, and this expense ratio is to be added to the loss ratio. These figures, nevertheless, speak volumes to a surety executive and must be

interesting even to a layman for they set forth in a nutshell the theory on which the business was founded and the satisfactory results obtained even under adverse conditions, for 1917 was an extraordinarily unsettled year from a labor standpoint, the changes on our schedules showing an enormous turnover of employees in the service of large corporations. And unsettled conditions and hard times tend to increase the number of embezzlements. These figures clinch the arguments so far as *bonded* persons are concerned. While we decline to write many applicants, we also do not have the opportunity of bonding millions more of gilt-edged risks. So I consider my general statement true both of the "bonded" and the free.

COST OF PRODUCTION.

The fact that one default will be equal to many thousands of dollars of premiums and that there are a few undesirable risks intermingled with the good ones has made necessary the most painstaking effort to weed out the dishonest from the honest. The size of the loss ratio is a very large factor in our "cost of production." We concentrate our efforts in keeping it low so that our product may be sold at a price commensurate to the protection rendered and within the means of every employer of labor. To accomplish this we must make a most careful selection of risks. We have no intention of declaring a man honest and reliable if he is not. Not if we know it first, and we usually do. Our bond means too much as an asset to the worthy to have it discredited, and mistakes in judgment do not do us any good either. So we evolved our present system.

Each new applicant for a bond is given a blank to fill out and sign, on which he is asked to tell: the date and place of his birth; what he has been doing for the preceding 10 years by year, employer, location and position; gives references (generally five); the full names and addresses of family, relatives and relations; information regarding his financial responsibility; the position to be filled and salary paid; his debts; the number of persons dependent upon him for support; whether or not he has ever been discharged from any position or gone through bankruptcy. These questions are not all, only some; but these give an idea of the information asked for. There is a reason for every question and we are not able to accurately pass upon the risk submitted unless each question is answered and answered fully. In this connection, the first part of the questionnaire filled out last year by men in the draft age was, as I recall it, similar in many respects to the standard form of fidelity application, and it is of interest to note that the Government proceeded to elicit its searching inquiry for purposes of classification along the lines blazed by surety companies.

Simply to give an idea of what these questions stand for I will take and enlarge briefly upon the last two in the preceding paragraph, viz.: discharge and bankruptcy.

If a man has been discharged from a position we want to know why. He needn't fear that we will forget that there are two sides to every controversy. We know that. But we know also that most employers are fair to employees in their reports to us; more give accurate and just answers to our queries than the applicant employees themselves. Occasionally unfortunate happenings arise in which an employee cannot clear himself, though innocent, from a cloud, and we receive conflicting statements from previous employer and applicant. In such an event I am safe in saying that our company will give a young fellow the benefit of a doubt every time provided his past record (the controversy in question excepted) *is clean*. If it is not clean his own past, not any action of ours, convicts him.

BANKRUPTCY.

With regard to bankruptcy, my own opinion of the ability of a man who has compounded with creditors is rather skeptical. A man who has mismanaged his own business may mismanage the business of the employer with whom he later affiliates himself. I should not care to issue a heavy bond upon a man occupying a responsible managerial or executive position who had previously been in financial difficulties unless I were submitted the facts and found there were extenuating circumstances. Bankruptcy casts a shadow upon ability and honesty, and everybody knows it.

People with whom we are brought in contact often tell us (though we know better than they) "There is no risk on bonds." Others say, "Your premium charge covers the risk on all bonds," which of course is not correct. Our premium charge covers the *selected* risks of each particular class. And still others say, "There is an obligation on you to sign my bond if it is all right." With this contention, especially as it pertains to fidelity bonds, I am inclined to agree. While primarily business organizations, formed for profit with the right to pick and choose our customers at will like any other corporation or class of corporations, the corporate surety bond stands for so much that American surety companies owe a duty to American business men to bond them if they are deserving. An unwarranted declination of an application means too much to the applicant to have it turned down without good solid reasons. A declination by us may make it extremely difficult, if not impossible, for him to secure his bond from any other company, for one of the questions to be answered on the standard blank is, "Has your application for a bond ever been declined by a surety company?"

If a prominent company has declined an application other surety companies regard the applicant with suspicion, assuming, and rightly too, there must have been good cause for the first company's adverse action. We owe it therefore to ourselves and to all men to regard and treat all applicants with absolute justice and all applications in strictest confidence, and I am glad to say that this spirit of fair play actuates our surety company executives, underwriters and agents.

What we preach to others we long since took seriously to ourselves, for there is no need to debate that well-known surety axiom, "The company that guarantees the honesty of others must be honest itself."

In touching in a brief way, as I have, upon the value of a clean record I have had the young man in mind more than any one else. Perhaps, because his life is before him to make or mar and because self-control is a product of age and experience, and young men lack both. There is such a magnificent future for this country in the world's affairs, and such a wonderful heritage for our young men to grow into as leaders of the world's greatest nation—for our young men shall have to assume responsibilities such as their fathers never dreamed of—it is tragic to think of their throwing *needlessly* such glorious opportunities away. I am doing them a service, therefore, if I urge them to be most careful in the handling and use of other people's money. Long experience in passing upon fidelity applications and in investigating the reasons for bonds having been declined has convinced me that it is impossible to be too careful. I recall now a recent instance in Boston where a man employed by one of our banking institutions was requested to resign because of his pernicious habit of borrowing small sums of money from fellow employees. He sought employment in another bank, and when he applied to the surety company on the schedule bond of that bank's employees, it unearthed a petty borrowing record on the part of this man extending over a period of years, and it declined to bond him, with the result not only that he lost that position but that he became blacklisted with all Boston banks, for all bond their employees. He couldn't secure a bond from any company; therefore became ineligible for service in any of the banks.

And along with this advice is a bit of warning. Let them keep constantly before them Bulwer Lytton's well-known statement, "Never treat money affairs with levity—money is character," because bonding companies—and bonding companies will go round the world to get their man—bonding companies, I say, and the Spanish proverb both truthfully assert, "Live with wolves and you will learn to howl."

PUBLIC OFFICIAL BONDS.

A Nation-Wide Menace to Taxpayers—Danger of Accepting Individuals as Sureties.

By Frank J. Menig, Superintendent, Public Official Department, National Surety Company, New York

One of the principal duties which the business man owes to himself is that of protecting his property and interests from loss. In line with his duty he insures himself and his business against fire, burglary, and other contingencies and places his employees under bond. The State has a duty quite analogous to that which devolves upon the business individual, i.e., that of protecting against loss the communal interests of its citizens and taxpayers. This obligation brings with it manifold responsibilities, foremost among them being that of requiring for officials entrusted with the handling of money, sufficient bond guaranteeing the proper discharge of their duties and the honest accounting for the funds thus coming into their hands.

Accordingly it becomes the duty of the State executives to require sufficient bond of its State treasurer, comptroller, superintendent and heads of the various administrative departments such as banking, insurance, highway departments, etc., and the officers in charge of State institutions such as hospitals, prisons and reformatories and such other officials who are responsible to the State government. The county board of commissioners or supervisors must see to it that its treasurers, tax collectors, sheriff, court clerks and other officials which compose the county government are sufficiently bonded. Similarly, it is necessary that the city, town and village government exercise the same duties as to their treasurers, collectors and other money-handling officials.

It would be expected that the same amount of bonds, relatively, should be exacted of money-handling officials where the duties of the office, the amount handled and other conditions are relatively the same. A study of the situation, however, reveals a wide and rather perplexing divergence of practice and regulation in this respect. It is remarkable to note how varied are the laws and requirements of the several States, and the views of administrative authorities as regards the sufficiency of bond necessary to fully protect the interests of the people against loss occasioned by defaults on the part of its servants.

STATE TREASURERS.

A particularly striking and typical example of insufficient bonding of public officials will be found in the case of various State treasurers. The treasurer of a large eastern State, whose office handles $35,000,000 of taxpayers' money every year, is bonded for only $50,000. In another great State, the treasurer handles $14,000,000 annually and is bonded for only $600,000. The treasurer of a western State, although handling $30,000,000 annually, up to recently was bonded for only $100,000.

The State treasurers of fifteen States of our forty-eight are bonded for a total of $4,015,000, and these fifteen treasurers have the supervision and control over the handling of $191,500,000 of public funds every year. If a large defalcation, approaching the total annual handling of any one of these officials should occur, the loss to the taxpaying public would be tremendous, because of the insufficiency of bond required on these officials. The treasurer of a southern State some years ago defaulted for $230,000. His bond had been executed by irresponsible bondsmen from which the State recovered only $60,000, leaving a net loss approaching $170,000 to the taxpayers.

DUTY OF BOND-APPROVERS.

In a few States the statutes require an official to give bond in the full amount or sometimes even double the amount of money handled during the year. In other States it is left to the discretion of the governing board, or the court having jurisdiction, to prescribe the amount of bond necessary. Unless the statutes specifically provide the amount of bond to be given, and lay down the qualifications of the sureties: a twofold duty devolves upon the governing party which is required by law to approve the bond; namely, (a) to see that the bond required is in a sufficient amount to meet any loss for which the official may be responsible. (b) That of determining whether the surety or sureties have adequate qualifications to afford the required protection. As to the first point, it should be remembered that the liability on the bond of a public official is not confined to his honesty alone, for he is responsible also for the honesty and proper performance of duty on the part of deputies and assistants in his office. Unless such assistants are sufficiently bonded, therefore, it will be seen that the heavy liability attaches to the bond of the chief official. This was demonstrated in the case of the tax collector in a city near New York a few years ago, where the surety paid a loss of nearly $9,000 due entirely to a defalcation committed by his deputy who was not bonded. Moreover, in many States the officials are responsible for the solvency of banks in which they deposit the public funds. It is clear, therefore, that various elements of liability should be considered when fixing the

amount of an official's bond, aside from that of his personal honesty. With regard to the second point, i.e., qualification of sureties, it is hardly considered necessary to point out the danger of accepting individuals as surety upon a public official's bond. The State or the public have no control over the assets of the individual who goes surety upon an official's bond. In most States he may dispose of his property as he pleases. Thus there is always danger when a loss occurs the individual may not be qualified to meet it. In fact, when an individual signs a personal bond, he does not anticipate a loss, whereas the surety company is in business for that purpose and is prepared for losses. Moreover, the doings and finances of surety companies are subject to frequent examination and investigation by the State and Federal insurance department.

DANGER FROM INDIVIDUAL SURETY.

The possibility that individual sureties may die before their liability has entirely expired creates a further chance of loss on the part of the public. A few months ago it was announced, through the newspapers, that the attorney general of a western State would bring suit against the several former State treasurers for the return of money embezzled by a defaulting bookkeeper in the State treasurer's office, who committed suicide three years ago. The newspapers made further comment upon the situation as follows:

"The names of some of the State's most widely known financiers appear among the bondsmen of these treasurers. A number of them have died since they were on the bonds, * * *." It would appear as though the attorney general will have some difficulty collecting from the remaining sureties unless the ex-State treasurers, under whose administrations the default occurred, make good.

This dangerous situation does not exist in the State offices alone, there are many county and city officials handling vast amounts of money who are insufficiently bonded. An instance showing the lack of uniformity is found in the case of the comptroller of a large eastern city, who gives bond of $300,000, whereas the treasurer of a smaller western city gives bonds aggregating several millions. As the finance department of the eastern city handles several times as much money as that of the western city, the difference in the amount of these officials' bonds is rather incomprehensible. It is a common occurrence, especially in the eastern States, to find treasurer, tax collectors and other officials, who handle hundreds of thousands of public money, bonded for perhaps $25,000 or $50,000. In some of the western States, county treasurers and tax collectors are frequently required to give bonds in very small amounts as compared to the extent of their public trusts.

GOVERNMENT EMPLOYEES.

The question of sufficiency of bond is frequently regarded as an unimportant detail in government administration which does not require serious consideration until a loss occurs and investigation reveals the fact that the defaulting official's bond is not sufficient means with which to meet the full loss. It is frequently discovered that the amount of bond was decided upon years ago for one of the predecessors in office, and was regarded as a fixed precedent, although the amount of money handled by the official has since multiplied many times over.

A few weeks ago the assistant treasurer of a southern town was found short about $15,000 according to the statement of the certified public accountant who had been checking the books. Since he was bonded for only $5,000, it would seem as though this town will probably be on the losing side for about $10,000. Last year a town treasurer in Rhode Island absconded, after having stolen $35,000 of town funds. He was bonded for $7,500, making a loss of about $27,500 to be sustained by the town.

Sometimes the fact that the official was elected by a majority of the voters or "selected" by the chief administrative body of the community, is regarded not only as a fitting endorsement of his character, but as a guarantee of his future honesty as well. The further fact that he is of the same political complexion as the approving board or court is generally regarded in his favor, when fixing the amount of his bond and the qualification of the surety. In the "toss up" between the public weal and frail human nature, the latter is given the benefit of the doubt.

INHERENT HONESTY.

That every man is inherently honest holds good with the politician and office-holder as well as the man in private life. Few people are born "crooks." Most of the losses paid by surety companies are the result of unintentional "borrowing." Nevertheless, such "borrowing" money is just as much of a loss to the victim, whether it be the surety company or public or an individual, as the pilferings of the thief who steals with malice aforethought. It would not be amiss to add in this connection that in some respects a man in public office is subject to stronger temptations than the private individual. Whether appointed by the administrative board of the community or elected by popular vote, the official invariably becomes indebted to those of his constituents who assist him in securing the office; the extent of the indebtedness depending upon the amount of assistance rendered. Sometimes these obligations are incurred to designing politicians who will endeavor to have the official do something derogatory to the interests of the public.

About two years ago the treasurer of one of the villages of New York State became short in his accounts due to the failure

of the bank in which the village funds were deposited. The treasurer had no financial means to reimburse the village for the loss. His bond, as approved by the village board, had been signed by the owners of the defaulting bank, this having been done, of course, for the purpose of securing the treasurer's deposit. One of the bondsmen had died and the assets of the others had vanished with the collapse of the bank. The village consequently lost about $5,000, following which they passed a resolution requiring corporate bond for all officials at the expense of the village.

CORRECTIVE LEGISLATION.

Widespread loss to taxpayers, through the insufficient or irresponsible bonding of public officials and the danger of taking personal surety on such bonds has caused progressive legislatures in many States to attempt reform measures, realizing that corporate surety is the sine qua non for an independent administration on the part of the officer in the service of the public, and these States have during the last few years passed laws permitting officials to give corporate bond, the premium thereon to be payable out of public funds. As evidence of the attitude of legislatures the following statement will be found appended to bill No. 77 introduced in the Senate of New Jersey in 1916, providing that where a public official files corporate bond the premium shall be payable by the State, county, municipality or school district, as the case may be:

"This Act will afford greater security to the State and the several counties and municipalities, and greater freedom to the public officials. Personal sureties are not infrequently of questionable protection to the taxpayers, not only because of their liability to financial reverses, but also because of the political influences they exert. The public official is also handicapped and rendered less efficient by being placed under obligation to personal sureties."

In his message to the Twenty-eighth Legislature (1917), the governor of Nevada made the following recommendation:

"Certain State and county officers are required by law to give official bonds in varying amounts for the faithful performance of their respective duties. There are good reasons why these bonds should be supplied by surety companies rather than by individuals. It is undesirable that public officials be under such obligations as are created by the securing of individual sureties. In the occasional instances when, in the past, it became necessary to collect on the individual bonds of public officers in Nevada, nothing has resulted but vexatious and fruitless litigation. The State should require surety bonds and should appropriate the money necessary to secure them."

PUBLIC OFFICIAL BONDS.

Educating Office-Holders in Corporate Suretyship—Neither Bank nor Agent is Proper Surety in All Cases.

By Thomas S. Dugan, Kentucky State Agent of the United States Fidelity and Guaranty

As corporate surety has now become so well established in this country, it would seem that everybody should be perfectly informed as to the advantages of corporate surety, but it must be recognized that they are not so informed. On each recurring election, the men elected to the several state, county and municipal offices must be separately and individually educated to the importance of their official bonds and the advantages of corporate surety thereon, just as though it were an entirely new proposition. The first and foremost point of importance is that an agent should be thoroughly informed and perfectly saturated with the arguments to be presented to the man who has been elected or is to be elected to a public office.

He should be prepared to present to the prospect all the reasons why he should not give a personal bond, one of which reasons is, that, by permitting his friends to qualify upon his official bond, he is placing himself under an ever-enduring obligation to his friends.

INTEGRITY IS ESSENTIAL

It matters not how many favors he may render to them, he is still under the obligation which he assumed when he permitted them to sign his bond as surety. Second, that he should not be willing for his friends to effectually mortgage their property by qualifying as surety upon his bond, which they certainly do, as the fact remains that while they are surety, their property does not belong to them. While the friend may appear to be, and in fact may really be, ever so willing to sign the bond, he cannot help from having some slight misgivings as to whether or not he should do so. If he tells his wife about it, she is sure to realize that he has assumed an unknown liability, for which he has received no compensating return, and that in event of the bad faith or misfortune of the principal, their home may be taken from them, purely as the result of an act of kindness on the part of the personal surety.

We are often told that the bank qualifies as surety upon the bond of the sheriff or the clerk or the judge. We, of course, know that the bank, as such, has no legal right to qualify as

surety upon the bonds of an official, and for the active officers of the bank to qualify as surety on such a bond would certainly not have the approval of thoughtful and careful stockholders, whose financial interests are in the hands of those active officers.

ENDORSEMENT BY BANK

It certainly would not be desirable for the entire board of directors of the bank to sign these bonds. Yet it would be eminently unfair for some of the directors to pledge their personal estates and the other directors not to do so. It seems to me that if I were a stockholder in a bank whose officers signed official bonds as surety, I would immediately endeavor to dispose of my stock in the bank at any price which I might be able to secure.

If an official should be so unfortunate as to suffer a loss upon his surety, even though it might be without purpose on his part, but by reason of some unfortunate condition in the discharge of his duty—for instance, a sheriff being forced to kill a man and then not being able to show that he was warranted in doing so—it can be easily pictured that a very heavy loss to the sheriff, far beyond his financial strength, would have to be borne by the surety, which might mean that one or two men would be forced into bankruptcy and the other members of the board of directors, if it happened to be that directors had signed the bond, would suffer no loss at all.

AGENT NOT QUALIFIED.

The agent should explain to the prospect that a man to be strong enough financially to qualify as surety on an official bond must be a considerable taxpayer. Therefore, for him to sign a public officer's bond would be placing himself in a position to be accused of exerting, and the official of yielding to undue influence, a very embarrassirg position for both.

It should be borne in mind and the fact presented that in the event of the death of the personal surety during the term of office, the adjustment of the entire estate of the surety would be materially interfered with by reason of the suretyship. The official would be embarrassed by being forced to seek other surety. Both conditions should be avoided.

SURETY COMPANY ARGUMENTS.

A surety company knows no personal conditions, desires no preferred influence, is permanent and unchanging in its existence, has been paid in advance for its services and for its own protection, furnishes the official with the service of an expert accountant from time to time during his term of office to see to it and make sure that the office is being properly conducted, and that the public monies are being directed to their proper

channel and not diverted therefrom. This service alone, it would seem, should be worth the premium, even if the official paid it out of his salary. The personal sureties themselves could better afford to pay in cash their pro rata of the premium charged by a surety company, rather than to sign their names to these official obligations.

As good business men, bank officials, merchants, farmers and property owners generally should recognize the reasonableness of these propositions which they have probably not heretofore thought of in just this way.

THOROUGH CAMPAIGN ADVISABLE.

If our agents will make memoranda of these several points, presenting them not only to the officials themselves, but to persons who would ordinarily be willing to qualify as surety on official bonds, letting each of them think how much more comfortable he would be during the official term of office to have a surety company on the bond, we believe that the practice of personal surety on official bonds would become a memory. While we recognize that the advantages of corporate surety are more generally recognized than formerly, at the same time we know that a constant campaign of education is absolutely necessary, as the personnel of officials is constantly changing. Accordingly, our agents should be reminded to preach this sermon yearly in order that the ever changing official family and the ever changing personal surety be educated on this most important subject, as are the school children educated from year to year after they arrive at school age and progress from one grade to another.

SURETY PROBLEMS IN WAR TIME.

Contracts of All Kinds Subject to Abnormal Conditions—Increased Hazards Result.

By Daniel N. Gage, Secretary Fidelity and Surety Department, Ætna Casualty and Surety Co.

Business interests throughout the country are now confronted with serious problems and with little certainty as to problems to be met in the future as a result of the great war in which this country is engaged.

The surety business generally, and particularly the contract business, is susceptible to whatever effect these abnormal conditions now have or will have in the future on the business interests of this country, and as a consequence we must exercise the greatest of care, precaution and conservatism in our underwriting in order to avoid serious losses.

We will outline herein briefly the increased hazard resulting on the more important classes of business from the abnormal conditions which prevail as we see them; the additional and extraordinary care which should be accordingly exercised in underwriting, and such changes in rates as have been made or are contemplated.

FIDELITY BONDS.

Increased Hazard. Many employers will not enjoy the same prosperity during the war as a result of the nature of their business as in normal times. They will accordingly curtail expenses as far as possible and the employees retained in many instances will not receive an increase in compensation commensurate with the increased cost of living.

Other employers will have an abnormal business requiring a large increase in the number employed and the same care will not be exercised in the class of help employed.

Other employers will lose for service to the government employees whose positions will be difficult to fill and many changes will occur as a consequence on schedule bonds with resultant increased cost to the sureties and less care in selection on the part of the employer.

Underwriting. In the investigation of applicants for fidelity bonds you should exercise care to see (1) that their past record entitles them to confidence in the position of responsibility they are undertaking to fill; (2) that they are receiving an adequate compensation for their living requirements, taking into

due consideration prevailing conditions; (3) that their past record of employments is complete and clear.

Rates. Where possible the bureau will make some increases in the rates on fidelity bonds, and agents will be notified in due course.

COURT BONDS.

Increased Hazard. When a surety signs a court bond, such as an appeal bond, release of attachment bond, etc., it practically guarantees the note of the applicant, payable anywhere from one to three years from date, with interest and such costs as may accrue in the litigation, and it is obvious that abnormal conditions which prevail to-day materially increase the hazard to the surety on bonds of this character.

In the average case the ability of the applicant to meet the obligation when it matures depends entirely upon the continuance of his business in its normal course. If the financial condition of his business is such at the time the bond is written that he could easily meet the obligation; his business has advanced beyond the experimental stage; it is not of a speculative nature or subject to unusual conditions or privileges for its support, it is fair to assume in normal times the applicant will be able to meet the obligation when it matures.

In these days, however, with the conditions affecting any particular business, in many instances uncertain as to future developments and it being difficult and in many instances impossible to borrow money readily, it is obvious how materially the hazard of the surety is increased.

Underwriting. Bonds of this class should rarely if ever be issued now without cash collateral or its equivalent.

Collateral other than cash should rarely be accepted and then only upon the approval of the home office, because collateral which could readily be disposed of in normal times is difficult to dispose of now and in some instances it is impossible to dispose of it.

Furthermore, we have seen our best stocks reduced in market price as much as 50 per cent., and in accepting collateral other than cash a larger margin must be secured than in normal times and the home office should be the one to determine what collateral it is safe to accept and on what basis of value.

Mortgages are rarely accepted as security on these bonds in normal times; they must afford exceptional security to be acceptable in these times.

In these days little real estate is exchanging hands and no real estate should be accepted as security without full particulars of the property being submitted to the home office and the security approved as acceptable to the company prior to the issuance of the bond.

Where real estate security is offered we should have the same information concerning the property that any banking corporation would require and which our mortgage loan department would require if purchasing the mortgage as an investment for the company.

Rates. The premiums charged on these bonds are only adequate to cover the service rendered and theoretically are not calculated to cover losses in addition.

There will be no changes in the rates on these bonds, because the rates now charged are all that the business will bear, taking into consideration that bonds of this class are written only for the largest and strongest applicants without collateral security.

FIDUCIARY, INCLUDING PROBATE BONDS.

Increased Hazard. The only increased hazard to bonds of this class is the effect present abnormal conditions may have on business in general and as a consequence involve the fiduciary who is being bonded.

Underwriting. Unusual care should be exercised, therefore, in investigation of the applicant for any bond of this class and joint control should be waived only where absolutely necessary.

Unusual care should be exercised to ascertain if any going business is involved and no bond of a fiduciary should be written where he is to be responsible for the conduct of a going business without consulting the home office.

Rates. There will be some increase in the rates on this class of business, but none that will cause any embarrassment and the rates will be furnished as soon as the changes are determined by the bureau.

CONSTRUCTION CONTRACT BONDS.

Increased Hazard. The contract business is undoubtedly feeling the effects of the present conditions and has the most uncertain conditions confronting it of any of our lines of business. The reasons are the following:

First, Labor. Labor is difficult to obtain at any price, and this, of course, is the result of the unusual demands of the government and the manufacturing interests throughout the country, which are undertaking very large contracts for the government, many of which are on a cost plus percentage basis where the government is more interested in the dispatch with which the work is done than in the cost.

No contractor is safe in anything, but practically a prohibitive estimate for labor cost on a large contract which will run over a period of one year.

Second, Material. Material is difficult to obtain and unless a contractor has a firm contract with a responsible, reliable material house for all the material required on a given contract,

it is difficult for him to determine, if not impossible, the price, or anywhere near the price, at which he will be able to obtain the material necessary to fill his contract.

Third, Transportation Facilities. You are all familiar with the extent to which the transportation facilities of the country are taxed and the orders which the government has found it necessary on many occasions to give prohibiting shipment of certain classes of commodities.

Fourth, Banking Facilities. The banks are exercising extra precaution in making loans these days. In some instances they are not loaning any money to contractors and are even calling in outstanding loans.

Where new loans are made to contractors the bank is invariably requiring security, and as most every contractor on any contract of size requires financial assistance from his bank some time during the life of the contract, this is a most important matter for the surety to take into consideration.

Fifth, Contract Provisions. Another increase in hazards to the sureties, but not as a result of the present abnormal conditions, is the change in the laws in some States on some classes of work, obligating the surety not alone to a guarantee of the completion of the contract and the payment of all labor and material bills, but in addition the payment of all bills for machinery, plant and equipment and other debts, which might readily be construed to include loans from banks.

The increased liability referred to in the preceding paragraph is not alone forced upon the surety through statutory provisions, but also through the insertion of such provisions in contracts, bonds and specifications by attorneys, architects and engineers who draw up the contracts.

There is an ever increasing tendency on the part of attorneys, architects and engineers to so broaden the scope of liability of the contractor and his surety as to make it absolutely essential for underwriters to review carefully the terms of contracts, specifications and bonds prior to undertaking to give the bond.

Some contracts contain provisions permitting any modifications without the prior consent of the surety, which means a contract of $50,000 may be increased to two or three hundred thousand dollars; terms of payments changed, etc., all of which materially affects the liability of the surety. Some contracts contain drastic provisions as to penalties for delays beyond the control of the contractor, which is a very important item at all times and particularly at this time, when a contractor may be delayed indefinitely in the fulfillment of the contract through causes entirely beyond his control.

In fact, at this time no contract should be bonded which obligates the contractor to penalties of consequence in the event of delays beyond his control, and all contracts should be specific

in their provisions that the contractor will not be held for delays which are beyond his control.

Underwriting. In normal times a contractor taking a contract at an upset guaranteed price allows for a profit of from 10 to 20 per cent. It is rare that he is able to obtain work which is desirable on a larger margin of profit. A margin of from 10 to 20 per cent., while adequate in normal times, is very possibly inadequate to-day because of the uncertain conditions which the contractor is likely to meet.

The result is that the better contractors are largely confining themselves to cost plus percentage work, except in those rare cases where they are able to obtain a contract on an unusual margin of profit basis.

Companies cannot afford to write bonds on contracts with an upset guaranteed price these days without the most thorough and careful investigation, and then only for those contractors who are sufficiently strong financially to stand a reasonable loss should contingencies arise which result in a contract with a loss of from 10 to 20 per cent. instead of a profit in that amount.

Companies have competent engineers who can pass on the adequacy of the bid price of any contractor who applies for a bond, if given the proper information, and cases should be referred to the home office with the necessary data to be reviewed by the engineers even where the case is one on which agents have authority to underwrite the bond without consulting the home office, unless the applicant is of unusual financial responsibility or there is no question whatsoever as to the adequacy of his bid and the desirability of the business.

The information required by company engineers is the following:

(a) The effect the location has on the cost of the work;

(b) Copies of contract and specifications, filled out as they will be executed, and the drawings;

(c) What and how the contractor estimates the cost of labor and materials on each of the items;

(d) Why he is able to bid lower than his competitors;

(e) What work will be sublet and the bids obtained from subcontractors.

In any case which an agent passes upon without consulting the home office he should obtain the following information:

First: Late financial statement of contractor and verify same.

Second: List of contracts under way and verify through engineer or architect in charge, and from contractor's books and records, that the same are progressing satisfactorily and are on a profitable basis, regardless of changes in labor and material prices since the contracts were taken. If the agent does not use

care in this matter profits from a new contract which he bonds will be applied to losing contracts under way and result in a loss under the contract bonded.

Third: Agent should investigate carefully the bid price on the contract he is asked to bond to satisfy himself that it allows for a sufficiently large margin of profit to assure completion even in these abnormal times at a profit.

Other bids should be compared; engineer's estimates should be carefully looked into and the engineer under whose supervision the work is to be done should be consulted.

Fourth: All sub-contracts for material should be carefully investigated, and unless the larger contracts are with thoroughly responsible material houses the bond should not be written.

All sub-contractors, unless of unusual financial responsibility, should be bonded, and the bond should be on the same broad form as the bond which it is proposed to sign for the general contractor.

Where the company has extended to the agent lines of credit on certain contractors, the agent should bear in mind the conditions which prevail to-day in contrast to those which prevailed when the line of credit was extended, and even if the time limit specified in the line of credit has not expired, he should consult the home office on any case where the bond is in excess of the underwriting authority in the underwriting agreement, and even where within his authority he should make careful investigation of the case in question; other work on hand and present financial condition of the contractor as outlined above.

Attention has been called above to some contracts where the additional liability is imposed upon the surety of guaranteeing machinery, plant and equipment bills and other debts. In all cases where this obligation is imposed the bond should never be given without first consulting the home office and calling to its attention such increased obligation.

Rates. As a result of the increased hazard to the surety on construction contract bonds, and as a result of the increased cost of the conduct of our business similar to that of every other business, the rating bureau has advised and put into effect an increase of 50 per cent. of the present rates in all manuals on all construction contract bonds, including maintenance bonds where contracts are taken at an upset guaranteed price.

This rate does not affect supply contract bonds or construction contract bonds where contracts are taken on a cost plus percentage basis with no guarantee as to maximum cost.

The agent should notify immediately all clients of the increase in rates so that they may be protected on any new contracts they may estimate and should in all such cases request their acknowl-

edgment of the receipt of the notice of the increase in the rates and ask them to agree in their acknowledgment of your notice that the two communications constitute a modification of the general contract agreement in so far only as the rates are concerned.

In any cases where indemnitors on the general contract agreements are had, new agreements should be signed providing for the new rates.

SUPPLY CONTRACT BONDS.

Increased Hazard. The increased hazard to the surety on supply contract bonds, while not as great as on construction contract bonds, is nevertheless material and the general uncertain conditions affecting all business interests will apply on this line of our business.

Many concerns are undertaking work for the government of a character which they never undertook before. This means a hazard to the surety which it does not experience on supply business in normal times, and in such instances our present rates, frankly, are inadequate.

Those concerns even which undertake work for the government of a character with which they are familiar are running their plants under great pressure and labor and material confronts them with serious problems.

Underwriting. The very low rate which applies on supply contract bonds will in itself appeal to agents as proving that it is necessary to exercise unusual care in underwriting these bonds.

The ability of the applicant to perform the contract he proposes to undertake should be most carefully investigated, including his sources of supply of labor and material.

Where the contract involves a class of work which the applicant has not undertaken in the past, the bond should never be written without consulting the home office.

On some of these contracts advanced payments are made to assist the contractor in equipping his plant with new machinery and in making additions, and no bonds should be issued where advanced payments are to be made without consulting the home office.

Rates. The rates were recently changed on this class of business, and as the great bulk of these bonds are now given to the United States government, no change is contemplated in these rates at this time.

OTHER CLASSES

Other classes of bonds will not be touched on specifically, but agents should bear in mind that present conditions affecting business in general affect all lines and they should govern themselves accordingly in the care exercised in the underwriting of all clasess of bonds.

Whether or not there will be any changes in rates on the other classes of bonds not specifically mentioned above cannot be predicted at present. While the abnormal conditions which prevail necessitate extraordinary precautions in underwriting, as suggested, the increase in rates is necessary because of the increased cost of the conduct of the surety business and it is only natural for the public to expect our business to be affected as has every other line of business been affected, and the cost of our service to be increased in reasonable proportion.

FIDELITY BONDS AND WAR CONDITIONS.

Service the Basis of Competition—Investigations Should Be More Thorough.

By C. E. Porter, Assistant Manager at San Francisco for the Fidelity and Deposit.

Fidelity business is considered desirable by surety companies, and perhaps written more widely and with greater leniency than any other class of bonds. But in these abnormal times fidelity bonds cannot be underwritten too carefully. Investigations of the applications particularly cannot be made too closely.

The surety company is placed in a peculiar position, because up to the present time success in building a fidelity bond business depended largely upon the service given. The keen competition for the larger lines of business induced companies to deliver their bonds in many instances before complete investigation of the applicant's record could be made.

I believe that if the war conditions continue much longer, surety companies will come to the realization that to write fidelity bonds profitably greater care must be taken in the

INVESTIGATION OF APPLICATIONS,

particularly in lines of business and industries essential to the war and enlarged by it. These industries are places of refuge for floating labor seeking the attractive wages and by employees of non-essential and undesirable occupations forced into the essential war industries by "Work or Fight" orders. In regard to these employees the surety company cannot be too careful. In the extensive operations and the enlarged plants, questionable people succeed in getting positions of responsibility.

The draft has had a telling effect on business. Everywhere we see offices, shops and stores operated with little or no efficiency, owing to inexperienced and incompetent help. Concerns are hampered by this class of help, and consequently their records cannot be kept accurately or their checking systems maintained strictly as in normal times. Most business houses are obliged to operate with elasticity. This condition is giving opportunity to the cunning and tricky individuals, who are enabled by the scarcity of labor to obtain positions of trust. An employer in these times is a prey for such individuals.

The shortage of labor is placing the employer in a helpless position, and prevents him from making a selection of help,

and with the increase of business he is obliged to seek protection through the surety company. The burden therefore ultimately is thrown upon the surety company. It must

EXERCISE CARE

in its investigations and underwriting or disaster will follow. Heretofore in normal times whatever losses we suffered have been on men whose records proved satisfactory and who were selected risks. One can therefore realize the importance of conservatism in these times with labor conditions as they now exist.

Then there is this point to remember: Many employees are now underpaid; the cost of living is higher due to the war (if not due to the war, the reason is nevertheless generally attributed to it) and the wage scale outside of the war industries is not in many business lines advancing correspondingly. Furthermore, in addition to this, greater demands are made than ever before in the way of subscriptions and contributions, to aid the war. This must not be overlooked by the surety company, for under such conditions "the strong grow weak and the weak, weaker."

It was remarked the other day by a judge of one of our local courts, handling criminal cases, that he was surprised at the number of embezzlement cases coming before him, where persons attributed their downfall to the numerous contributions they were obliged to make out of their salaries. Whether or not patriotism was injected into the case to justify a criminal act, or with the end in view of seeking leniency, could not be determined with certainty. It is a condition, however, which might reasonably exist.

THE FUTURE

of our fidelity business, however, is not to be viewed with pessimism, because the war has created favorable conditions as well for the surety company. As the draft was constantly taking men, the employers were obliged to place women in positions of responsibility, which heretofore have always been occupied by men. Our experience with fidelity bonds on behalf of women has been very good, and I believe I am safe in saying that the experience of other companies has been the same.

SURETY BONDING AND SELECTION.

Credit Element—Importance of Selection—Value of Complete Data—"Rush Service" Unsatisfactory.

By Wilmot M. Smith, Manager Fidelity and Surety Department, New York Branch, Ætna Casualty and Surety Co.

The business of building a large fidelity and surety premium income is no different from any other kind of building. You must first obtain the services of one well schooled in the art and the science of building; second, lay out your plans; third, get your materials together, and last and most important of all, get busy.

Among the numerous insurance agents in this country, there are very few who have obtained any prominence as producers of fidelity and surety business, because the writing of bonds, while generally associated with the insurance business, is handled on an entirely different basis of underwriting.

A great majority of bonds are credit obligations; only a few are in the nature of insurance. The premiums are based generally as "service charges," and this causes our business to be much misunderstood. Applicants fail to understand why they should pay a premium and then give complete indemnity. This situation is misunderstood by the ordinary insurance agent as well as by the applicant.

The agent or branch manager who succeeds in producing a volume of profitable bond business is one who not alone understands the business from the standpoint of the field man, but who is working in close co-operation with the home office and presenting to the underwriter the necessary and essential information concerning each risk. The value of the producer with the company and his ability as a bond-man, is determined by the resourcefulness and judgment displayed in presenting his various cases in such shape as will permit the home office underwriter to determine the merits and demerits of the particular business.

When a risk is declined, it is very generally the fault of the field man in not knowing how to present a case in underwriting shape for his home office. The business is generally good. It will undoubtedly be written by some company. Many good bonds are declined by the home office every year, simply because the underwriters do not know what they should know about a case. A great many bonds are declined because the field man

attempts to secure "rush service" in order to obtain a piece of business, and after gathering the essential facts, rushes a wire to his home office requesting authority. This method of doing business is usually explained to the applicant by the field man as rendering "service." The general result is that a wire does not obtain facts, but instead mostly generalities, consequently the application is usually declined and the agent spends an unpleasant half hour trying to explain to the applicant why his bond has been disapproved.

The agent who will eventually obtain the business and who undoubtedly is the most successful agent at that particular community has not been rushed, but has gone into the proposition in an intelligent manner, has gathered the essential information and data and has presented the case to his home office in complete shape. The result is, that when his home office receives the papers, they are in a position to give the application intelligent consideration, and invariably are in a position to wire their approval, and then Mr. Agent communicates with the applicant, advising him that his bond is ready for delivery. This approval may have been received several days after the application was received, and the applicant has secured what he has applied for, and has not received a declination such as he had received from those agents who wished to give such favorable service.

The successful agent should sit steady in the boat and pick his business. Usually the most hazardous risks are those which are generally in sight. Leave them alone. Go after the safe business. Don't ever recommend to the company a risk you would not accept yourself. The secret of success of building a volume of fidelity and surety premiums depends to a great extent on the confidence which the home office has in your ability and their assurance that you are not only submitting the favorable aspects of the case, but also those features which do not appear so attractive.

The average field man fails to appreciate the importance of having all papers pertaining to a bond risk completed and properly executed. It is well to realize that there is a possible lawsuit at the end of every bond term. Have your application blanks and indemnity agreements properly filled in and executed in a legal manner. The general insurance agent does not appreciate the importance of this feature. The application not only supplies the data upon which the risk is underwritten, but constitutes the surety's grounds for reimbursement when a loss has been paid. An error or omission in an insurance policy or application might prove a kindness to an insurance company, but not so with a bond. The bond application may contain a multitude of misstatements, errors and omissions, yet the bond is good and must be paid if a loss occurs.

If the field man will grasp the fundamental fact that the fidelity and surety business is one of credit and not one of insurance, will present in every instance to his home office complete underwriting data, present only such cases as he personally approves, picks his business and follow his company's requirements, then there is no reason why an insurance agent cannot develop a substantial bonding business.

THE SURETY APPLICATION.

Surety Bond Questions Answered for Agents—What the Underwriter at the Home Office Wants to Know About Risks.

By Marc Hubbert, Contract Bond Department, National Surety Company.

Some months ago, while discussing what should be done in the way of encouraging and educating representatives of surety companies generally, an agent remarked: "You know I have often wondered why certain questions are asked on the applications, and if you can get up some form of communications which will give us fellows who haven't time to sit down and "bone" the thing out, the reasons why the information asked for is required, I believe your efforts in that direction would be rewarded."

Then and there it was resolved to try out the suggestion. The result was the preparation of a series of "Explanations of Applications" in which the various questions are propounded and the reasons given for wanting the information.

In preparing the original "Explanations" in order to make the plan effective, all the questions asked on each application were commented upon, but in presenting them herein, for the sake of brevity, repetition of the reasons for asking the questions which are manifestly obvious will be omitted.

The application blanks of but one company were used in getting up this material, but since there is so great a similarity in the application blanks used by all of the companies, it will be easy for the agent for any company to apply the reasons for asking the questions to the forms with which he is familiar.

Your pardon is asked if the "Explanations" seem too long for many of you who have a knowledge of the business, but you must remember this information has been prepared for those who may be novices, and who are interested enough to sit down and read it through, so that they may hold their own with you "fellows" who already "know how."

Another thought about these "Explanations." Don't get the idea that they represent the "Gospel" of all companies, for it would be next to impossible to give an accurate composite expression of the way they all look at the various subjects treated upon, but the author believes he has "toed the line" as nearly as could be done under the circumstances.

Imagine yourself to be the underwriter at the home office, who is to pass upon an application. You are hundreds of miles away from the place where the business originates; have no personal acquaintance with the agent, the applicant, or his financial responsibility, or of the references, and yet wanting to give the best possible attention to the business, if the information on the application blank is given only in part, and perhaps indifferently so, what is your duty? Is it not first to the company, and to decline the risk if time will not permit of writing for the omitted data?

The "Explanations of Applications" gives you the "Reasons" why the questions are asked. They have been prepared so you may inform yourself as to the companies' requirements, and if you will carefully observe them, you will find the correspondence both before and after the execution of a bond will be greatly reduced, with a consequent economy of your time and of those at the home office; to say nothing of having fewer declinations of applications submitted.

Before proceeding with the "Explanations," kindly permit one general remark, which you should bear constantly in mind. It is: that there are a multitude of different kinds of fidelity and surety bonds which can be written for your clients, and that it is a great mistake for an agent to confine his efforts to soliciting but one or two lines, because periods of depression, or other influences, may cause the demand for a certain class of bonds to drop off altogether; where on the other hand, the agent who has placed a great variety of bonds, will have his income maintained regardless of the general conditions.

OFFICIAL BOND

The questions to follow are asked in the application blanks used by practically all of the surety companies.

It is hoped the ground herein is fully covered, and that the "Reasons" for asking for the information will prove to be correctly and clearly stated.

Usually there are two forms of applications used for official business, designated as the long form, and the short form. The former being used in all cases where the official wanting the bond will collect or disburse money. The short form is to be used "For Public Officials whose bonds are not in excess of $5,000 and who do not handle money."

Inasmuch as questions on the short form also appear on the long form, it is deemed unnecessary to give reasons for asking for the questions in any but the long form.

Q. 1. Name of applicant. Residence. Married or single. Birthplace. Age.

R. 1. The company must have applicant's full name for use in preparing the bond. A misstatement of the name of the

official in the bond might prevent him from qualifying in the time specified by law. The other questions must seem to be obvious.

Q. 2. To whom bond given.

R. 2. A misstatement of the name of the obligee in the bond might cause trouble to the principal, and perhaps delay giving approval of his bond, thus preventing the official from qualifying until correction has been made. It's easy to do things right in the first instance, so be painstaking in handling all details.

Q. 3. Official title of applicant.

R. 3. The statutes usually define the duties of each official, hence the mention of the official's title will in most instances give a fair idea as to his duties. In the newer localities, however, some of the officials are acting in a dual capacity, so give the company the exact facts regarding the duties of the office. The duties of city officials are prescribed by charter and ordinances. Send copy of city charter to the company at the time you submit applications for bonds for city officials.

Q. 4. Elected or appointed. When term begins. Length of office. By whom appointed or elected.

R. 4. This is for use in preparing bond, and involves making a correct recital of facts in the bond, such as "whereas on the 1st day of May, 1913, John Smith was elected (or appointed) to the office of city treasurer of Jones Falls, Montana, for a term of one year from the 1st day of June, 1913," etc.

Q. 5. Duties and responsibilities of position or office.

R. 5. This form of application is used for taking information regarding bonds wanted for almost all classes of officials, their deputies, and other employees in offices of municipalities. Unless the duties of the applicant are defined by the statutes, it is necessary to have a recital of the work he is to perform and under the direction of what official or governing body.

Q. 6. Do you collect taxes—State, county, municipal.

R. 6. In many States where officials or their deputies collect taxes, if the collections are not made the official is held responsible for such omission, hence the surety company wants to know if the applicant's duties embrace such liability.

Q. 7. State amount of each duplicate. When will duplicates be placed in your hands for collection. When due—when in arrears.

R. 7. The answer here will determine the extent of the official's responsibility and furnish data from which the company may know within what periods the taxes must be collected, and suggest the proper time for making inquiry to learn whether or not the official has been doing his duty in the matter of enforcing collections. Inquiry will disclose the fact as to whether

or not the official has an undue amount of uncollected taxes on hand and when payments of such shall be deemed in arrears.

Q. 8. Collection of poll or head tax; fines and forfeitures; license tax.

R. 8. The answers to these questions give the company positive information regarding duties of officials, and must be furnished. Many bonds are wanted for city officials, and others, whose duties are not defined by statutes, and, too, their duties are changed from time to time so that it is almost impossible for the surety companies to keep pace with the changed instructions except by making special and specific inquiry of the applicant.

Q. 9. Liability for uncollected or delinquent taxes.

R. 9. The matter of responsibility of the official for uncollected taxes was touched upon above. If he is responsible the company wants to make sure that the official fully understands that such is the case.

Q. 10. Relief from such liability.

R. 10. If the official is relieved of responsibility for uncollected taxes by a provision in the statutes, his answer will determine whether or not he is aware of the law. If reply shows that he is not, the company may want to communicate with him and set him right on that score.

Q. 11. To whom and when will you make report of insolvents and delinquents.

R. 11. The statutes or ordinances will govern, hence this question asked, so the company may know if the official understands his duty with respect to reporting delinquencies.

Q. 12. What is your compensation.

R. 12. The company must know what the principal's income is, and that he receives it at satisfactory frequent intervals.

Q. 13. By whom is premium paid.

R. 13. The company wants to know to whom it must look for payment of the premium. If the municipality pays it, it will be necessary to present the bill at the first meeting of the commissioners, council, etc.

Q. 14. Deputies employed. Will bonds be required.

R. 14. The official who must employ deputies is usually responsible for their acts, therefore, the company must know for how many deputies the official's bond may be liable, and whether or not the applicant (official) understands the extent of his liability. If not, the company should and undoubtedly will bring the matter to his attention, and see that he exacts a bond from each deputy. Incidently will say, because the official trusts his deputies, implicitly, is the very reason they should be bonded. The

trust so imposed affords the opportunity to make away with funds entrusted to their care. Experience shows that many a trusting official has been "wiped out" financially by the acts of his deputy. Consequently no company can afford to run the risk of its principal getting into trouble, when just a bit of precaution will afford ample protection.

Q. 15. Amount of money handled. What month receipts largest. Time largest amount under control.

R. 15. The company must know how big a proposition it has been asked to bond, and determine the question as to whether or not the applicant's previous employment has fitted him to conduct the duties of the office. When receipts are largest the company will want particularly to look to the matter of bank depository protection, and to determine the adequacy of same. You can readily see that the greater the amount of funds susceptible of being misappropriated, if carried continuously, the risk to the surety is correspondingly increased.

Q. 16. To whom, how often, and on what dates do you report receipts and disbursements.

R. 16. These questions are asked for various reasons, and when answered satisfactorily, in addition to giving the company information useful to it in preparing and keeping up its records of the risk, also give assurances that the official is fully aware of what the statutory requirements are respecting his office. If the applicant's answers indicate some doubt as to his knowledge of the law, the company may take steps to help him come to an understanding of his responsibility.

A surety company, especially in bonding an official handling money, must make systematic inquiry to learn whether or not he is rendering his reports and settlements according to law, hence much of the information asked for under this heading is to be used in preparation of cards necessary in a "follow-up" system to keep in touch with the situation.

Q. 17. Where official funds deposited.

R. 17. When the company knows in what banks the funds are to be kept, it must look up the credit rating of the institutions, and confer and advise with the official concerning the matter of depository bonds to be required of the banks to secure such deposits.

Q. 18. Is depository designated by law.

R. 18. If the depositories are designated by law, proper resolutions should be passed by the county commissioners, city councils, or other governing boards, so that the official will be distributing the funds in strict conformity with the law. Otherwise he may be held personally liable for any loss; so when an official can do business under such a law he should see that

proper resolutions are passed for his protection, immediately upon taking office.

Q. 19. By whom depository designated. Is bond liable for failure of bank in which deposits kept. What arrangements, if any, will you make to receive interest on deposits of public funds. State agreement, and with whom.

R. 19. If the official designates his own depositories usually he and his surety assume all the liability in case of bank failure. On this account the company must know that he is alive to the risk he is taking, and will see that he requires the banks to furnish ample and satisfactory bonds or securities to reimburse the official in case of bank failure. Some officials are a bit careless about this matter, or may feel safe in playing favorites in the matter of dividing up the deposits. This is a serious matter. Here is where friendship should cease, and the permission granted to the bank to keep part of the funds, put upon a cold business basis; that is, the official should require the banker to give proper security or get none of the deposits.

Q. 20. In whose name are deposits kept.

R. 20. No surety company will bond an official if it is aware of the fact that he proposes to carry the bank accounts in his individual name. If answer to this question indicates such a practice, the company must either have the matter adjusted so that the official's title will be included in the name of the bank accounts, or be compelled to decline the risk.

You can readily see that unless the funds are marked so as to be readily distinguishable from private funds, considerable trouble might be caused to straighten out legal entanglements.

Q. 21. Are funds withdrawn by check of applicant. Is countersignature required.

R. 21. The official usually signs the checks on the bank accounts, but where in his absence, or for other reasons, this is not always practicable, companies sometimes advocate requiring checks to be signed by two deputies, or if there is but one deputy in the office, countersignature of checks might be had by arranging with an official in one of the other offices of the municipality; city clerk, county clerk, county auditor, etc.

Q. 22. If funds are paid out upon orders of other officials, do their orders or warrants accompany or become part of your checks or drafts upon depository. Give particulars.

R. 22. The custom of permitting the banks to charge up warrants, or other demands against the municipality to the official's accounts, should not be encouraged, as such act may place both the bank and the official in embarrassing positions should the bank charge any unauthorized items to the account.

In other words, the official being held responsible for his office,

and liable under his bond for mistakes, whether his own or the acts of another, must be the one who will say whether or not the charge should be made against the funds in his custody. Officials who are held responsible for proper disbursement of public money should require all warrants and other drafts upon the accounts to be presented to their offices and the official's check on the bank be issued in exchange therefor.

Here is a good place to say a few words about the advantages of depositing all the receipts from whatever source, whether cash or checks, in bank as a matter of record, and not pay warrants or other items in actual cash, but make all disbursements by check. By pursuing this course the records will be more complete and the likelihood of mistakes being made reduced to the minimum.

In offices where a number of people are handling collections of taxes, etc., each one should have his separate cash drawer, and not have a number of clerks using a common cash box. Following the former course makes it easy to fix the responsibility for mistakes, where the "general" cash box invites "error" and may be a cause of much uncertainty and unfounded accusations.

Q. 23. Have you previously held this position. During what period. Bond furnished—why change desired. Has been canceled or an application declined by any surety company. Give particulars.

R. 23. The expression "hold-over official" is used so frequently, and since it applies to one who has "previously held this position," it is well at this time to give a definition of the term:

A "hold-over official" is a person who, having finished the term of office for which he was elected or appointed, having been re-elected or reappointed enters upon his second or subsequent term with but little time elapsing between such employment. The writing of a bond for such "hold-over" official, who handles money (these comments do not apply to officials who do not handle money), unless bonded for the previous term by the company to which he applies for a bond for the succeeding term, is not regarded as specially good business. In fact, some companies are altogether opposed to accepting such risks, because the official has so many ways by which he may juggle his accounts for the previous term, and thus place all the liability upon the bond covering his acts in the succeeding term. Surety companies, therefore, cannot, except in rare instances, engage such "hold-over" risks; when they do so it is only after an examination of the accounts of the official has been made, and everything seems to be satisfactory.

Further, even though the official's accounts do appear to be

entirely regular, should loss ensue and, although as a matter of fact the shortage occurred during the first term, if a change of surety is made at the beginning of the second term, and the surety on the second bond is unable to show that the loss did actually occur during the first term, the second surety is liable and must pay. Do you wonder that the surety companies will hesitate about taking the risk. Of course, you must be governed by the attitude your company takes towards the "hold-over" risks. If you would have such risks accepted answer every question propounded, fully and clearly, and you will find the application will receive prompt attention, where considerable correspondence will result if important information is omitted. The reasons for asking the remainder of the above questions would seem to be obvious.

Q. 24. What was your employment prior to the acceptance of the position for which bond is desired.

R. 24. It does not follow, because a man has been elected to fill a public position that he is fully qualified to administer the affairs of his office.

The facts are that many of our public officials are not so qualified, and while the public, by ballot, may decide that John Smith will make a very acceptable county treasurer, in looking over application for his bond, the company may determine that on account of his lack of clerical and other general business experience, it cannot afford to take the risk, for the surety would be liable for both his dishonesty and loss through carelessness or lack of ordinary good business judgment.

Q. 25. Will you continue in any business or employment during your term of office. If so, state character of same, and probable net income per annum.

R. 25. Constant attention to the duties in some official positions is not always required. In fact, the compensation will not justify so doing. The official, therefore, is often compelled to engage in some other pursuit, and such a situation must be understood by the company If the business, or other employment, is not satisfactory to the company, it might think best to decline the risk.

Information as to the income from other employment will help to determine whether or not the official is earning enough for his needs.

Q. 26. Do you own property—real or personal. Amount of debts, etc.

R. 26. The necessity for having the above information is so obvious, special comment here would not seem to be necessary. Suffice it to say, applications for bonds are turned down by the score daily, because the person wanting the bond will be evasive

about making a statement of his assets and liabilities. The applicant who lists only a part of his property, when turned down, will forever damn the surety company; whereas, he really was entitled to the bond, and would have gotten it if he had made a full and clear statement of his finances.

Many applicants object to making a complete statement of their assets and liabilities, because they imagine the company publishes it to the world.

As a matter of fact the company guards confidential information of that sort just as sacredly as does a bank withhold knowledge of any of your dealings with it from the public. If such were not the case no company could remain long in the business. There is scarcely a corporation of any consequence, and thousands of individuals and firms, whose statements have gone on file with the various surety companies without any hesitation, so that the prejudice some people have against making a full statement is due largely to lack of knowledge of general business usages.

See that the amount of the premium is inserted in the space provided therefor in the agreement of indemnity.

BANK FIDELITY INSURANCE.

Loss Distribution—True Loss Ratios—Maturity of Experience—Evil of Underinsurance.

An Address by R. H. Towner, of New York, before the American Bankers' Association, at Chicago, September, 1918.

At the outset of any discussion of suretyship on bonds, including bank fidelity bonds, certain differences between insurance and suretyship must be noticed in order that the subject may be understood. Ordinarily, the relation of insurance includes two parties only: the insured who pays the premium and the insurer who receives it. Suretyship is a relation of three parties. A surety bond is given by a principal who is primarily liable; his surety corresponds to the insurer; and the obligee on the bond corresponds to the insured. In suretyship, as distinguished from insurance, as a general rule the premium is paid by the principal and not by the obligee (the insured). On many of its important obligations, suretyship differs also from insurance in respect that the premium for suretyship is paid to procure credit rather than to distribute loss. On these classes of suretyship losses cannot be paid out of the premium fund alone. Sureties look, instead, to the financial responsibility or the collateral security supplied by their principal. These constitute the chief fund for payment of losses and their deficiencies are recouped out of premiums. But on bank fidelity bonds the principal is seldom of great financial strength; always insolvent when he is a defaulter; the premium is usually paid by the bank; and premium earnings constitute the fund out of which bank fidelity losses must be paid. Hence, bank fidelity bonds, differing from many other classes of suretyship, bring the surety company and the bank very closely to the simple relations of insurer and insured. They may be correctly classified as insurance policies.

LOSS DISTRIBUTION.

The function of insurance is to distribute loss. It collects premiums from an entire class of policyholders, each of whom is insured; and it pays losses to a few of that number who

suffer loss. By this means the losses of a few are distributed over all. There is a lateral distribution of loss when, in normal years, premiums paid by the whole body of policyholders equal the losses and expenses of that year. There is a longitudinal distribution of loss, through time, when the premium payments of favorable years are accumulated by the insurer and subsequently paid out in one or more years of unusual losses. This is accomplished by a level premium rate which makes an apparent profit when losses are small, to be eventually balanced when they are large. A lateral distribution alone would make premiums fluctuate from year to year as the loss experience changed.

How to fix a level premium rate which shall honestly and effectively distribute fluctuating losses over a long series of years is a question that interests both insurer and insured. The former wants to know that he is receiving premium enough to afford a sound basis for his underwriting calculations. The latter wants to pay only enough to keep his insurer solvent, but not so much as to contain an inordinate profit. The problem is beset with difficulties, some of which must first be explained.

THE TRUE LOSS RATIO.

Losses cannot be ascertained by inquiry from the banks themselves. Circular inquiries of that character are often answered inaccurately by banks which rely upon their memory, or whose management has changed. Many banks do not answer at all. And the most complete set of replies always omits those banks whose fidelity losses have been so heavy as to cause their failure. That is, the replies to such a circular come only from solvent and going banks. Banks which have failed as a result of defalcation do not receive the inquiry. The reported losses on such circular inquiries, therefore, bear about the same proportion to the true loss as would an inquiry on fire insurance which turned up only the small fires but omitted all the buildings which burned down.* The reductio ad absurdum of this method

*Parties interested in reciprocal fire insurance sent out a circular inquiry on their fire losses, to various New England shoe manufacturers early in 1917. When they checked up the replies, they reported that the fire insurance premiums paid by the manufacturers in the three years, 1914, 1915 and 1916 came to $131,120; and that the only fire losses in that period were $1,596.56. Thereupon, Mr. Gorham Dana, manager of the Underwriters Bureau of New England, gave a list of fire losses on shoe factories in 1914, 1915 and 1916, aggregating $986,400! See *New York Journal of Commerce,* February 19, 1917.

is seen when applied to losses on depository bonds. On this class of bonds there are no losses except by reason of bank failure. So that an inquiry addressed only to solvent banks discloses an apparent record of no depository losses whatever.

For the same reason, it is impossible to get the true loss ratio by inquiry of surety companies. Since 1907 more than a majority of all surety companies writing bank fidelity bonds have failed. The loss experience of all the failed companies is unavailable. Inquiries addressed to surety companies, therefore, disclose not the true losses, but only the losses suffered by the survivors. Wherever a large number of companies are continuously writing a like branch of insurance and some of their number from time to time fail, it is mathematically certain that a loss ratio derived only from the experience of the survivors will be necessarily incorrect. The true loss ratio is shown only by the experience of the whole number. Those that suffer the heaviest losses fail. So that the survivors' experience must always be more favorable than the experience of the whole; and if the profits of survivors equal the losses of failed companies, underwriters have just come out even.

Current losses also are inaccurate as a criterion of true loss ratios. A surety company begins business with no bank fidelity bonds. At the end of ten years its business has grown so that it has (say) one hundred millions of outstanding bank policies on which it has received premiums. Current losses paid by it to this date are only part of its losses. Its whole loss will not be found until these policies have matured and all claims upon them have been paid and extinguished. When it has thus ended, as it began, with no liabilities and no policies outstanding, its true loss ratio for the ten years may be computed.

Even on ordinary insurance the true loss ratio is often cunningly concealed in the fluctuations of experience; so that a very great period of time must elapse before the maturity of experience discloses it. In fire insurance this was well illustrated by the testimony of Mr. Charles L. Case, United States manager of the London Assurance Corporation. His company, he said, had remitted an average underwriting profit of one hundred thousand dollars from its United States branch to its London head office every year for forty years until the San Francisco fire. This was more than wiped out, however, by that disaster, on which his company paid losses of five million dollars. So that in a period of fifty years the average annual underwriting profits

of one hundred thousand dollars for each year would be exactly offset by the unusual loss of five million dollars in one year. This is the maturity of experience and illustrates how insurers must accumulate premiums to distribute losses over time. A like rule applies to suretyship. Normal years do not disclose the whole loss ratio. Provision must be made for abnormal years, and some part of the profits of normal years accumulated and reserved to meet abnormal losses.

MATURITY OF EXPERIENCE.

For surety companies the maturity of experience means more than it does for fire insurance companies. When a fire insurance company closes its books on the thirty-first of December it knows exactly what the fires of the past year have been. The past is plain, even if the future is hidden. A surety company, on the contrary, when it closes its books at the end of the year does not know even what losses have been incurred in the year just past. All large defalcations are made possible only because the defaulter can conceal his thefts for a long period of time. Surety companies, therefore, are often renewing their bonds and continuing their insurance for bank officers who, unknown to the bank or the surety, are, in fact, defaulters for large sums. These losses have already accrued when the bond is renewed. Eventually, they will be brought to light and must be paid. So that a surety company on the first of January is not only in the dark as to what its losses will be in the coming year, but it does not know even what its losses have been in the past year. No other branch of insurance combines so many factors of uncertainty.

"Maturity of experience," then, means for fire and other branches of insurance, where losses cannot be concealed, simply a cycle long enough to include the fluctuations of experience; a due proportion of bad years, as well as good ones. Unlike other classes of insurance surety companies have to pay losses that are long concealed; losses which existed in the years that are past, for which the surety companies books were closed, but which are discovered and result in claims in the years to come. Deferred losses of this character are peculiar to suretyship. In all other branches of insurance, experience fluctuates but is always known. In suretyship, it not only fluctuates, but is partly hidden. "Maturity of experience" for surety companies, therefore, means a period of time long enough to cover the fluctuations of known losses and to disclose hidden and deferred losses.

These claims are made and paid years after the surety has ceased to collect premiums.

Must we say, then, that true loss ratios on bank fidelity bonds are indeterminable, and that it is impossible to arrive at a correct rate? No, we need not confess our impotence to deal with this question simply because it is beset with difficulties. In the beginning, surety companies had little or no data as to losses. Premium rates were fixed at first by experimentation and competition. Current losses, never a complete guide as to what the premiums should be, at least served as a correction to those companies whose premiums were too low. Competition for business reduced the rates of those whose premiums were too high. So that, in the course of my memory in the surety business, bank fidelity premiums have fallen from 75 cents to the present rate of 25 cents per $100. The reduction is really greater because bond forms are now much broader and the "warranties" with which the old forms were filled are not now required. The correctness of this rate may be fairly inferred from the fact that no company writing an extensive volume of bank business at a lower rate can long survive. And no company charging more than this can obtain an extensive volume.

A VALUABLE ILLUSTRATION.

An unusual opportunity, of the greatest value to actuaries, has been lately afforded for the careful study of practically a complete cycle of fidelity and surety experience. The American Fidelity company of Montpelier, Vermont, which began business in 1901, extended its operations until, during the four years 1910 to 1913 inclusive, its premiums exceeded $1,000,000 a year, aggregating $5,852,587. Following the year 1913 it ceased writing certain large lines, and these lines have been entirely liquidated. For three years more it continued to write other lines on a smaller scale. These have now been likewise liquidated. And for 1917 its net premiums from all lines were only $11,000; a smaller sum than for any preceding year since 1902. Instead of liquidating through a receivership, where its losses were hidden, or where its insolvency forced claimants to a compromise, it has liquidated through its own officers, and its annual reports continue to be made. From these reports it is possible for the actuary to draw, with mathematical accuracy, conclusions as to the relation between current loss ratios and the true loss ratio, current experience and matured experience, on fidelity and casualty insurance. A summary of its annual premiums,

losses, expenses and the results for seventeen years is here presented:

TABLE A—COMPLETE EXPERIENCE OF AMERICAN FIDELITY COMPANY FOR SEVENTEEN YEARS—SHOWING ITS TRUE LOSS RATIO.

	Net Premiums	Losses Paid	Management Expenses	Losses to Premiums Per Cent.	Management to Premiums Per Cent.	Losses and Management to Premiums Per Cent.
1901...	$4,282	....	$1,598	.....	37.3	.....
1902...	5,898	23	6,831	.....	115.8	.....
1903...	13,549	818	15,904	6.0	117.4	123.4
1904...	34,602	5,295	24,698	15.3	71.4	86.7
1905...	191,765	30,974	104,856	16.1	54.7	70.8
1906...	309,627	101,986	139,589	32.9	45.1	78.
1907...	329,790	100,529	153,600	30.5	46.6	77.1
1908...	423,693	184,198	193,638	43.5	45.7	89.2
1909...	637,357	168,978	265,132	26.5	41.6	68.1
1910...	1,002,780	322,851	390,910	32.2	38.9	71.1
1911...	1,900,069	711,408	606,269	37.4	31.9	69.3
1912...	1,706,289	1,314,211	694,884	77.0	40.7	117.7
1913...	1,243,449	1,482,336	513,789	119.2	41.3	160.5
1914...	300,883	613,280	245,507	203.8	81.6	285.4
1915...	313,786	466,609	202,371	148.7	64.5	213.2
1916...	161,500	269,125	134,208	166.6	83.1	249.7
1917...	11,333	115,690	69,935	1021.	617.	1638.
	$8,590,652	$5,888,311	$3,763,719	68.5	43.8	112.3
Unpaid Claims, Dec. 31, 1917	....	193,155	....	.....	....	.....
Total Losses..	....	6,081,466	....	70.8	....	114.6

TABLE B—PARTIAL EXPERIENCE OF AMERICAN FIDELITY COMPANY FOR SEVEN YEARS; EXTRACTED FROM TABLE A—SHOWING FALSE LOSS RATIO.

	Net Premiums	Losses Paid	Management Expenses	Losses to Premiums Per Cent.	Management to Premiums Per Cent.	Losses and Management to Premiums Per Cent.
1905...	$191,765	$30,974	$104,856	16.1	54.7	70.8
1906...	309,627	101,986	139,589	32.9	45.1	78.
1907...	329,790	100,529	153,600	30.5	46.6	77.1
1908...	423,693	184,198	193,638	43.5	45.7	89.2
1909...	637,357	168,978	265,132	26.5	41.5	68.0
1910...	1,002,780	322,851	390,910	32.2	38.9	71.1
1911...	1,900,069	711,408	606,269	37.4	31.9	69.3
	$4,805,081	$1,620,924	$1,853,994	33.7	38.6	72.3

To the paid losses of $5,888,311 there is added in Table A the net unpaid claims shown in its annual report as of December 31, 1917, amounting to $193,155; making a total of $6,081,466. Adding in $3,763,719 of Management Expenses gives a grand total for losses and expenses of $9,845,175; against which there were received in seventeen years, premiums of $8,590,652. The combined losses and management expenses, therefore, exceeded its premiums by $1,254,523, representing the money lost by this company in its underwriting operations for seventeen years. During this period its underwriting policy was consistent and unchanged. Its investments were good, its management was honest, and its management expenses were normal. Disaster overtook it because its premiums were too low.

Much that is disclosed by the American Fidelity company's experience table has long been known to careful students of fidelity and surety underwriting. The table simply presents this information in mathematical formulae. In the long period of fluctuating loss ratios, finally mounting to figures which spell insolvency, we see no changes of underwriting policy, good underwriting followed by bad, but merely the effect of deferred losses finally overtaking insufficient premiums. The years of heavy loss ratios were not due to inadequate premiums for those years alone. They show that the underwriting results of previous years failed to fortify the company with accumulated reserves equal to its deferred losses.

How unreliable current loss ratios are as an index of true loss ratios is clearly shown. If current losses even approximated the true loss ratio, they would tend to oscillate around it, being sometimes more and sometimes less. The table shows, however, that this did not take place. Only once during the seventeen years does the current loss ratio bear any likeness to the true loss ratio. For eleven years, the current loss ratio remained persistently below the true loss ratio, and for six years it was far above it. While the current loss ratio was low, current losses were met. When its experience matured and current losses were augmented by deferred losses, the true position of the company became known. The table exhibits the results with the greatest clearness. Some of the lessons to be learned from it are the following:

WHEN LOSSES MATURE.

1. Surety underwriters have long known that losses follow two or three years after premiums are written. The table makes this plain and fixes the maturity date for losses with surprising accuracy. The peak of the American Fidelity company's premium earnings was reached in 1911, when premiums were $1,900,000. The peak of its losses, however, was not reached till 1913, when losses were $1,482,000. Its losses, therefore, were at least two years behind its premiums. This is shown again by another test. Its 1914 premiums were but one-fourth of its 1913 premiums. That is, they dropped from $1,243,000 in 1913 to $300,000 in 1914. But there was nothing like a similar drop in losses. Losses for 1914 were approximately 40 per cent. of 1913, nearly half 1912, and nearly equal to the 1911 losses, when the company's premium earnings were $1,900,000, against 1914 premiums of only $300,000. To find a point where losses dropped to one-fourth, it is necessary to compare the losses of 1915 and 1917. The former were $466,000 and the latter $115,000. Hence, again we find that the cut in premiums between 1913 and 1914 is not reflected in a like cut in losses, until we compare the years 1915 and 1917. By this test, therefore, as by the former, it appears that losses do not mature until two or three years after premiums are written.

CURRENT LOSSES AND CURRENT PREMIUMS.

2. With this data, observe how misleading are current loss ratios. After the year 1904, the company began to grow rapidly. As premiums increased each year, its losses increased in a smaller proportion. But its annual reports for these years show a comparison of current losses with current premiums, resulting in the low percentage shown in Table B. It is now evident, however, that current losses compared to current premiums show ratios that are pure fiction. The loss ratio of any one

year never, except by chance, coincides with any company's true loss ratio, since the latter is the combined average of many years. But if the losses of any one year are compared with the premium earnings of two years earlier they will, in surety underwriting, furnish a much nearer approximation to the true loss ratio. Comparing the losses of one year with premium earnings of the same year in a rapidly growing company leads to no true results at all. It cannot be even approximately correct. It is simply a mischievous illusion.

How the American Fidelity company was misled in this respect is clearly shown by the table. Its loss ratio at the maturity of experience was 71 per cent. But for seven years, 1905-1911 inclusive, it had an apparent loss ratio which never exceeded 43.5 per cent. and averaged only 34 per cent. During all this time the company thought it was prosperous. Its business was increasing, its apparent loss ratio was low, and its directors actually declared and paid dividends out of its imaginary "profits." In fact, during all this time it was losing money. It was deceived by the false comparison of current losses with current premiums. Had it compared its losses each year with the premiums of two years earlier, the illusion would have been dispelled.

CURRENT LOSSES VS. TRUE LOSSES.

3. Not only the time necessary for deferred losses to mature, but the amount of these losses is ascertainable with approximate accuracy. At the end of 1911, the American Fidelity company was eleven years old. It had reached the peak of its premium earnings and its apparent prosperity. More than one-half of the total premiums shown in the table had then been written—$4,863,000 out of a total for seventeen years of $8,590,000. But much less than one-half its total losses had then been paid—only $1,627,000 out of $5,888,000. At this period, then, it had received 56 per cent. of its total premiums and had paid only 28 per cent. of its total losses. Its loss ratio at the end of 1911 was only 34 per cent. of the premiums which had then been written. This loss ratio, when its experience finally matured, was 71 per cent. So that in the first eleven years of its history its current loss was slightly less than half the true loss ratio shown when its experience matured. In the remaining six years it had to pay $4,261,000 of losses while it wrote only $3,727,000 of premiums. This result was not due to a sharp change in the company's management or underwriting policy, for its management and policy remained the same. Its apparent loss ratio at the end of 1911 was purely fictitious. Instead of the apparent 34 per cent. it was really 71 per cent. And the deferred losses which created an illusory prosperity in its first eleven years engulfed its earnings in its last six years.

4. The management expenses shown in the table come to an average of 43.8 per cent. of premiums for the whole seventeen years. This is a reasonable figure for any company writing large general lines. For a company specializing on a small line, the management expenses would probably be higher. It is customary to treat as "Management Expense" all of a company's disbursements not included under the head "losses." This custom is too old to be broken by me. Those unfamiliar with surety underwriting, however, should be told that "Management Expense" in reality includes a great deal of money which the company never sees; and considerable more which it must pay out by law. The money which the company does not see is the agents' commissions. These vary, but a fair average is 25 per cent. This is never remitted to the insurance company's treasury, but stays in the town where the premium is written. Most States have resident agents laws intended to compel the companies to do business through local agents and to secure to local agents their commissions. The picture of loss ratios which is obtained by employing as a denominator the premium written on the face of the company's policies is, in fact, erroneous. The denominator should, in reality, be 75 per cent. of that premium since only 75 cents out of a dollar ever reaches the company's treasury. This is often overlooked by the insured, but it is always a fact. It is sometimes overlooked by investors in new surety companies, who are surprised to find that while the real loss is double the apparent loss, the real premium is only three-quarters of the apparent premium.

Solvent bonding companies show their experience curve only to the point where their outstanding liabilities are maintained and annually increased. Failed companies hide the remainder of their curve in receiverships. The American Fidelity did neither. Its figures are necessarily chosen because they afford to the actuary his only opportunity to follow a complete cycle of experience to the end. But it was engaged in general lines of fidelity, surety and casualty underwriting. How then, does its experience on general lines aid the actuary in the accurate computation of a level premium rate which shall truly reflect the fluctuations of experience on bank fidelity bonds alone? These bonds were only part, perhaps a small part, of the company's general business. The answer is that there is a distinct advantage in computing underwriting results on a large field of risks over a long period of time. Fluctuations of experience which affect separate lines of underwriting with considerable violence, are absorbed when the area of experience is broadened to include many lines. The separate fluctuations of different lines tend to offset each other, so that the unfavorable

experience of one is balanced by the favorable experience of another. Underwriting results may be computed with mathematical accuracy only when the field is large and the time is long. When thus computed they are applicable, with equal certainty, to every part of the underwriting field.

DEFERRED LOSS ELEMENT.

Our task, then, of finding a level premium to cover the fluctuating experience of Bank Fidelity Bonds is greatly aided by the general experience of the American Fidelity company. Underwriting conditions surrounding these bonds are similar to fidelity and surety risks generally. In some degree they are accentuated. Bond forms approved by the American Bankers Association contain no "cutoff" clause limiting the time for claims. Continuity of protection is given, so that bankers may collect losses when discovered, regardless of when the thefts took place. Familiar examples of deferred losses will occur to every one. In the Alvord case, an employee of the First National Bank of New York, stole from the bank for thirty years, his thefts aggregating $700,000 before discovery. A similar case with a loss almost exactly as much occurred in Philadelphia only last year. Recently, also, it was discovered that the President of the Chemical Bank of New York had defaulted for nearly $300,000. The discovery was not made until after his death. Like cases will be recalled in almost every large city of the country. Hidden and deferred losses, therefore, added to the normal fluctuations of known experience, always and everywhere accompany bank fidelity underwriting.

As bankers bonds share the general conditions surrounding fidelity underwriting, their premium rates are subject to the same mathematical rules. The time necessary for the maturity of experience; the mathematical relation between current loss ratios and the true loss ratio; the proportion which deferred losses bear to current losses; all these factors, brought out with such extreme clearness in the examination of the American Fidelity Company's completed experience, affect Bank Fidelity Bonds in no lesser degree than other lines of fidelity and surety underwriting. All that we have learned of the underwriting results of the general class may be safely applied to this special class. Much more safely, indeed, than if we had been able to study the limited and special field of this line alone. For, as I have before remarked, the narrow field of a single line is subject to fluctuations too great to be accurately reduced to mathematical formulae.

We can apply, then, the experience of the American Fidelity Company to the problem before us. From their exeperience, we can compute a current loss ratio bearing such a relation to the true loss ratio, that when experience has matured, when all

losses have been paid, and all liability extinguished, the insurer shall come out even. On that basis general fidelity rates are established. In near correspondence to them are the rates for Bank Fidelity Bonds. Observing their current loss ratios from year to year, we see that, with some fluctuations, they average about twenty-five per cent. higher than current loss ratios on other fidelity lines. This we know to be the extreme limit of difference compatible with sound underwriting. To let current losses on this special class exceed the ratio to premiums which is now reached, would cross the danger line pointed out by experience. The problem of a level premium rate, beset with difficulties as I have said, is yet not insoluble. As far as experience can guide us, we know that our present premium rates are accurately computed and reach a correct result.

LOSS RATIO ON BANK BONDS.

One or two prevalent errors respecting Bank Fidelity Bonds should be noticed before I conclude. One is that loss ratios upon them are unusually low. It is true that compared to the face of the policies, bank bonds show a small proportion of loss. But this is accurately reflected in the lower premium rates at which they are written. When losses are compared to premiums received, the underwriting results on Bank Fidelity Bonds show current loss ratios about twenty-five per cent. higher than on other fidelity lines. So that where other fidelity lines assure the underwriter a reasonable certainty of profit, on Bank Fidelity Bonds the profit is by no means certain. Current loss ratios continually approach, sometimes pass, the danger line indicated in the experience of the American Fidelity company. Any surety company whose underwriting was confined to Bank Fidelity Bonds, would face occasional years of serious loss, with few years of considerable profit. By averaging them with general fidelity lines this danger is greatly diminished. Narrow areas of underwriting are always subject to sharp fluctuations. A broad field absorbs fluctuations, offsetting unfavorable experience on one line with favorable experience on another, so that reasonable stability results.

It is likewise supposed, in some quarters, that the premium rates on Bank Fidelity Bonds are higher than on other surety underwriting of a less desirable class. Occasionally, it is said that surety companies which charge $2.50 a thousand on bank bonds, charge only $2.00 a thousand, or less, for Tax Collectors. Wherever this difference exists it is due solely to the fact that by statute Tax Collectors are required to give bonds equal to or double the whole sum of taxes which they collect. Wherever this is true, there is a certain amount of over-insurance on the Tax Collector's bond. He could hardly steal the whole sum of his collections; and even if he did it would not reach the penalty

of a bond which is double the amount of the tax roll. This overinsurance is taken into account in fixing rates. A level premium is charged for the whole of the statutory bond. But that part of the premium allocated to the actual liability on the bond is far higher than the rate charged to banks. To make this plain, suppose the tax roll were $100,000 and the Tax Collector's bond $200,000. On this bond a premium rate of $2.00 per thousand comes to $4.00 per thousand on the entire amount of collectible taxes. These same taxes when paid into a local bank are but a small part of its deposits. And these taxes with all the rest of the bank's deposits are often protected by fidelity bonds not exceeding $50,000. Thus, the complaint that the rate for the Tax Collector's bond is less than for the bank bonds, is wholly unfounded. At $2.00 a thousand a Tax Collector has paid $400 for suretyship on his collections. At $2.50 a thousand the bank has paid only $125 for fidelity bonds covering the same taxes, plus all the remainder of the bank's resources.

EVIL OF UNDERINSURANCE.

Underinsurance is a prevailing evil on Bank Fidelity Bonds. Where statutes require Public Treasurers and Tax Collectors to be bonded for the whole sum which they handle, banks normally require their officers and employees to be bonded for only a small fraction of the money they can steal. In these cases the bank carries a large part of the risk itself. But the results on fidelity underwriting for surety companies are, that were losses on Public Official Bonds are usually smaller than the bond penalty which measures the premium, on bank bonds the loss is often total. One or two surety companies have prepared circulars showing in a striking manner how much bank defalcations often exceed their bond protection. One such circular now on my files enumerates specifically forty large defaults and gives the surety bond upon them. The aggregate total of these forty bonds was only $655,000; but the forty defalcations came to $8,592,000. This evil, necessarily reflected in fidelity underwriting results, is being gradually corrected, to the great benefit of the banks themselves, by the growing use of Blanket Bonds, which afford the bank adequate coverage. On these bonds there is a double measure of premium, so much for the penalty of the bond, so much for the number of employees, with an additional surcharge for branches. Blanket protection of this character is very advantageous to banks. The outcome to surety companies can now only be guessed at. The time during which they have experimented with it is still too short to warrant any conclusions as to underwriting results.

BROADER FORMS BRING INCREASED LOSSES.

In the examination of any figures of fidelity experience extend-

ing far into the past, this general caution must be observed: that the fidelity bond formerly in use was a narrow instrument, drawn with a view to protecting the surety in great measure from undisclosed and deferred losses. In recent years, banks have demanded broader forms; and these forms will show increased losses. This change, highly beneficial to the banks and accepted in good part by the surety companies, has been brought about largely by the activities of the Insurance Committee of the American Bankers Association. That committee has approved the present insurance rates, but has constantly and vigilantly exercised its powers in careful scrutiny of insurance contracts. It is due to the Insurance Committee to say that the forms of insurance contracts have been greatly improved by it; that better relations have been established between the banks and bonding companies; and that this improvement would not have been brought about by the individual action of separate surety companies. It was brought about by the Insurance Committee of your organization, which exercised uniform, wholesome, and perfectly legitimate pressure on surety and burglary underwriters.

These three factors must combine to afford proper security to banks: the premium must be adequate, so that insurers will be solvent; the amount of insurance must be proportioned to the bank's risk of loss; and the insurance contract must be so drawn as to be clearly understood and furnish sufficient coverage. The first factor I have discussed at length; the second is decided by each bank for itself; the third has been attended to by your Insurance Committee with eminent ability. On the whole, therefore, it may be said with truth, that bank fidelity insurance is now more stable, and the relations between surety companies and the banks are now better than ever before. A high standard has been reached and there is no reason to suppose it will ever be abandoned.

FIDELITY BONDING.

Investigation of Applicants—Warranties—Desirable and Undesirable Risks.

By E. E. Kolb, Superintendent of the Fidelity Section, Maryland Casualty Co., in The Budget.

In deciding upon an application for a fidelity bond, more weight is given to the statement of one former employer than to any statements that might be made by four or five other references. For our purpose, no person can know an employee as well as a man for whom he has worked; this applies not only to his methods of work, and to his ability, but also to his honesty. An unfavorable statement from a former employer, will usually cause the company to decline an application for a fidelity bond, even though all other reports are favorable, if the unfavorable report of a former employer goes so far as to state that the applicant has not been honest when handling money, or has at certain times temporarily withheld funds belonging to the employer. On the other hand, it must be remembered that one of the most difficult things to contend with in fidelity underwriting, is the weighing of investigations, and the deciding of how much credence to give to a report not entirely favorable. Our experience is that employers are generally very glad to give a deserving former employee the best sort of recommendation, but sometimes we get reports which make us suspect that the employer is inclined to be vindictive or spiteful, and cases occasionally arise where we are practically certain that the employer has not been fair to his former employee.

After completing the investigation of an applicant for a fidelity bond, the next thing to decide is whether it is advisable to issue the bond for the particular position held by the applicant. A fidelity bond is not intended to protect an employee who uses a faulty system of accounts, nor is it intended that simply by getting fidelity bonds, the employer can be careless in the choice of men.

Surety companies are now issuing a number of bonds that contain no warranties, but this does not imply that an underwriter is never to suggest to an assured the necessity of frequent examination of his accounts, combined with a close watch upon employees, so that any employee who might temporarily hold funds belonging to his employer will know that discovery will come almost immediately. As a usual thing, a thief is not made

in a day. Defaulters in most instances start in a small way, and tell themselves they are just borrowing a little of the employer's money. This alleged borrowing is very easy if the employer has a loose system of accounting, or never has his accounts audited carefully, and in the case of traveling salesmen, does not send bills directly to his customers. A careful underwriter, therefore, regardless of the form of bond executed, will suggest to the employer that certain checks and safeguards be installed, and while our rates do not directly take into consideration whether the employer does or does not keep a close watch upon the accounts of his employees, a conscientious underwriter will avoid risks where he has reason to believe that the accounts are not examined at regular periods. The rates for fidelity bonds on traveling salesmen are now so low that it is impossible to bond such applicants unless the assured sends regular statements directly to his customers. Most losses are found upon investigation to occur where there is either no system of accounting, or such an inadequate system of accounts that the defaulter found an easy method of beating the system: information as to the method of accounting in use, is secured through a statement from the present employer of the applicant.

The bonding of men who work on a commission basis, requires special attention. Practically all insurance agents are compensated in this manner, likewise consignees and brokers. In considering bonds for insurance agents who work on a commission basis, it is necessary to have the past record of the applicant, which often shows that he has been in the insurance business for a considerable time, and that he has established a reputation for steadiness that entitles him to a bond. It is much harder to decide whether or not an insurance agent who is just starting out, should be given favorable consideration in the matter of a fidelity bond; in such cases, if the applicant's record is good in every respect, and he has some property, there is no reason, if he has always met his obligations, to decline his application for a bond, especially if the insurance company, with which he is connected, is known to be well managed and makes frequent examinations of the accounts of its agents.

Bonds on agents of other sorts, and consignees working on a commission basis, are handled in a similar manner. In such cases, we are as much concerned about the standing and methods of the obligee, as we are about the character and record of the applicant. Consignees and agents who handle goods in carload lots, or who sell to dealers in large quantities, are usually desirable risks, but where the consignee or agent is really a retailer, the risk is much less desirable. That is, we prefer to avoid risks where the bond amounts to a guarantee that a retailer will pay for goods at wholesale prices when he has disposed of them at retail—after he makes his collections. The percentage of

trouble in cases of the latter sort, is so great that if we were to charge a premium which would make risks of this character attractive, the cost of the protection would be too high to make it salable.

We do not care to bond one partner of a firm in favor of another; one partner cannot criminally steal from another. There are so many disagreements in partnership affairs, that nothing other than a larceny and embezzlement bond should be issued, and the company prefers to avoid contracts of indemnity where it knows in advance that the bond actually carries no liability.

What we call isolated risks, that is, bonds in favor of single employees of large concerns whose other employees are all bonded elsewhere, are dangerous and undesirable. Such risks have generally been declined by the surety company that carries the other employees, and it is very reckless for an underwriter to risk his judgment on a new line against the judgment of the underwriter of the company carrying that line; occasionally an isolated bond shows a good experience, but the average experience on such cases proves that there is no money in this class of business.

FIDELITY INSURANCE CLASSIFIED.

An Interesting Method of Defining Hazards—Classification by Employers.

By John G. Yost, Assistant Secretary of the Fidelity and Deposit, in The Fidelity Journal.

Of all the various lines of insurance, fidelity business is probably the least sought after by agents. The principal reasons for this are the general lack of knowledge how to solicit fidelity business, an ignorance of the principles underlying its proper handling, and a failure to understand what a fidelity bond actually guarantees to the obligee. In order to simplify matters, we are calling this class of business insurance and shall endeavor to make clear the several classifications by referring to it in terms of fire insurance.

There are three main classifications of fire hazards, viz.: (1) the preferred business, which consists of dwellings and of household furniture; (2) mercantile risks; (3) manufacturing risks. In addition to your being in a position to underwrite these risks from the standpoint of the hazard involved, you are, to a certain extent, guided by the premium rate, the policy form being the same in each instance, with the exception of the various clauses and endorsements applicable to certain conditions peculiar to the particular risk.

Fidelity business, or fidelity insurance, as we have decided to call it, may also be divided into certain classes, which we shall call, for convenience, preferred, ordinary and hazardous. In the fidelity business, however, all three of these hazards may carry the same rate, while the discrimination between the risks is made, to some extent, at least, through the form of bond or policy issued. In other words, we *may* write a narrow form of bond for a hazardous risk at the same premium rate as we write a broad form of bond for a preferred risk. The class into which each hazard falls will be obvious to any insurance man.

The preferred class would naturally include officials, inside clerks, bookkeepers, et al., of strong and reputable corporations, banks, or other large concerns operating either as individuals or as partnerships. These employees are usually good, high-grade men who associate with proper people, are compensated by salary, assuring them a regular income, and who can look forward to advancement in their positions. In such cases we do not hesitate to issue a very broad form of bond.

The second, or ordinary class of employees, includes such risks as local or traveling salesmen, working on a salary, and inside salesmen working on a salary. For this class we write our form No. 940 (individual), or No. 985 (schedule), which is the standard form adopted by the Surety Association of America, the coverage under which is practically as broad as under forms No. 409 and No. 410, except that there is a pro rata recovery clause, and but six months is allowed, after cancellation, in which the employer may discover a loss. This form is also largely used in the execution of bonds for small concerns having only one bookkeeper or cashier, or one or two clerks.

The third, or hazardous class, is composed of drivers and collectors, specialty salesmen of every sort, solicitors, and, generally, all salesmen working on a commission basis.

CLASSIFICATION BY EMPLOYERS.

The underwriting of fidelity business is not confined to the selection of good risks from among employees. The employee himself, it is true, is the real risk, but the character of the business conducted by the employer must not be disregarded. There may be many employees coming within the preferred class of fidelity risks, working for an employer of the hazardous class, and vice versa. Also, an A1 man in a hazardous line, where the temptations are many, may be no better risk, from a surety standpoint, than a man not so highly regarded, in a preferred employment. But, as a general proposition, the class of employees may usually be determined by the character of business in which the employer is engaged. This enables us to underwrite risks from the standpoint of the employer, and greatly assists us in cases where it is possible to combine these two factors. As is the case with regard to the employee, it will also be obvious to which class of hazard the employer belongs.

The preferred class of employers consists of strong, reliable corporations, banks and large mercantile and manufacturing concerns generally. Such employers usually conduct their business in a systematic manner, the checks and safeguards being such that it is difficult for employees to steal without detection, and if they do, the system usually catches up the irregularities before they have gone very far, at least as to time, if not as to amount.

It is very difficult to define the ordinary fidelity hazards among employers, although they frequently occur. The nearest we can come to a rough description of the class is to use as an illustration a concern employing both inside and outside men, the outside or more hazardous risks being taken along with the officers, managers and the office force, thereby making the risk, as a whole, only ordinary, the hazardous offsetting the preferred risks.

Concerns, the majority of whose employees are drivers and collectors, commission salesmen (particularly those selling specialties), are included in the third, or hazardous, class of employers, even though they are high-class and responsible concerns. In this hazardous class are also laundries, bakeries, dairies, instalment houses and chains of stores selling a single or various commodities,—shoes, hats, etc.

UNCERTAINTY AS TO COVERAGE.

One of the principal reasons for agents not soliciting fidelity business more aggressively, is the lack of thorough understanding of just what a fidelity bond covers. It indemnifies an employer against losses sustained through acts of larceny or embezzlement only, in the narrow bond forms, as against loss from fraud, dishonesty, larceny, embezzlement, forgery, wrongful abstraction, wilful misapplication or misappropriation, in the broad forms of bond; and it covers not only the employer's money and securities, but also his goods, as well as any other person's goods and materials in the custody of the employer, and for which the employer is responsible.

Employers, when approached on the subject of fidelity insurance, admit that there are dishonest men in all walks of life. They have read of defalcations committed by the employees of other concerns, but they seem unable to get out of their heads the idea that all such stealings are of real money only. Newspaper articles, when reporting defalcations and embezzlements, refer to the number of dollars stolen. If employers knew that in many instances these dollars represented stolen goods and materials there would be more fidelity bonds carried by the small employers, as well as by the larger ones. As a matter of fact, we find that a great many surety agents are able to think of embezzlements and defalcations only in terms of actual money stolen.

A thorough understanding of the fact that these bonds cover anything of value belonging to the employer, or for which he is responsible, would probably make a great many surety agents more enthusiastic over fidelity business, with the result that the companies now doing this class of business in this country would be receiving far more than a total of but $8,000,000 annually in fidelity premiums. Think of but $8,000,000 in fidelity premiums being the total annual fidelity business in a country of one hundred million people! That is less than $1 in fidelity premiums written for every ten persons, and it is very doubtful if any one of us could think of ten persons without knowing one among them who holds a position in which he or she should be bonded, while, as a matter of fact, probably not more than one in seventy-five or one hundred is now under bond.

If, therefore, you will inform small employers,—such as furniture dealers, haberdashers, clothing stores, or other first-class firms, employing one or two clerks, as to the full coverage obtainable under fidelity bonds, there is no doubt that hundreds of applications for fidelity bonds could be secured, where the employer now carries no such protcetion. This would be of benefit, not only to him and to us, but also to the person bonded, as the very knowledge that a surety company is on his bond acts as a great deterrent to wrong-doing, and as an inducement to put temptation aside, when otherwise it might overpower him. To such men, the sordid consideration that honesty *is* the best *policy* may frequently be the deciding element in the struggle between temptation and the dread of punishment. Many men are honest, not because it is right, but because it is the safer course, and to such men the fear of the consequences is what frequently controls the decision.

JUDICIAL FINANCIAL GUARANTEES.

Thorough Investigation of Customer Necessary—Advance on Bail Bonds.

By L. C. Reynolds, Maryland Casualty Co., of Baltimore, in The Budget.

The principles underlying the handling of financial guarantee bonds are not difficult; cash collateral or its equivalent in marketable stocks or bonds, equal in amount to the entire sum involved, is usually required. If full collateral satisfactory to the company is secured in advance, there is usually no cause to worry. If the collateral rule be followed, any man of common sense can write bonds of this class. There is less to remember when considering the execution of financial guarantee undertakings than there is on administration cases, where you must consider the moral standing of the prospective fiduciary rather than his financial status. Almost the opposite of that is essential when underwriting financial guarantees. You are obliged to investigate thoroughly the financial standing of your customer, primarily, and his moral standing secondarily. If you find that he is not worthy of credit on any kind of a financial guarantee, the liability should not be assumed no matter how high he may stand morally in the community. He may be as honest as the day is long, yet could not pay a nickel should his case be decided adversely to him.

Surety companies divide what are generally called financial guarantees into two classes, namely: bonds for plaintiffs and bonds for defendants. The former is considered far less hazardous than the latter. Undertakings for plaintiffs are such as cost bonds, replevin, attachment, injunction, garnishment and petitioning creditors. The liability of a surety company on these classes is generally for cost of the suit and damages, in most instances, although damages are seldom proven; yet there have been many exceptions.

BONDS FOR PLAINTIFFS.

Some agents may not be familiar with the several bonds for plaintiffs, so a brief explanation may be advisable. For instance, the cost bond—when a person intending to bring an action in a court resides without the court's jurisdiction, the court or the defendant, previous to the issuing of summons, or at any time before the trial, requires such plaintiff to give security for the cost of the suit. The costs as a rule do not amount to more

than fifty or one hundred dollars, but sometimes they are far greater. It is usually difficult to secure collateral to cover liability on such cases. A good rule to go by is as follows: secure collateral covering estimated amount involved, providing penalty is not greater than $2,000, unless the applicant has a net worth of at least $10,000, over all liabilities and when the utmost liability under the bond cannot exceed twenty per cent. of such net worth.

The same rule applies to replevin, attachment, garnishment, petitioning creditors, libel and injunction. A replevin bond is one wherein the plaintiff seeks to secure the possession of property which he claims is unlawfully held by another.

An attachment bond applies to a case where a person has instituted legal proceedings to recover on an account which he claims due, and seizes property belonging to the defendant in order that he may recover in case judgment is secured by him.

A garnishment proceeding is one wherein a plaintiff endeavors to tie up funds in a bank or assets in possession of any third party in the event he secures a judgment against the defendant.

A petitioning creditor's bond is one wherein three or more persons join in a proceeding for the purpose of declaring the defendant a bankrupt.

A libel bond pertains to a case in admiralty in which the plaintiff attaches a ship or its cargo.

An injunction bond is one filed in a case wherein the plaintiff endeavors to prevent the defendant from doing or not doing a certain thing, as is set forth in his petition.

These are the principal undertakings which are known as "original process" bonds, and the rule as heretofore stated should always apply.

The opposite of these bonds are more strictly financial guarantees, and no undertaking of this class should be executed without collateral unless the waiver of such protection first be secured from the home office. They are: discharge of attachment or garnishment, release of replevin, appeal, supersedeas, stay of execution, indemnity to sheriff or marshal, and release of libel.

CREDIT GUARANTEED.

These bonds guarantee the payment of a judgment, or its equivalent, together with interest and costs. In other words, such undertakings save the plaintiff free and harmless from all loss, because the surety company guarantees the credit of the principal. Consequently the financial standing of our customers is the most important thing to be ascertained. We never permit ourselves to enter into the merits of the case. A surety company cannot act as judge or jury, nor can it foretell the outcome of the suit. If after careful investigation by the surety and its

agents it is not satisfied that the applicant will be financially responsible, three or four years hence, such risks should be declined unless cash collateral or its equivalent is deposited in advance. Collateral should be waived only in cases where the principal is a well-established corporation worth many times the penalty of the bond.

Surety companies and their agents cannot be too careful as to insisting upon complete protection before accepting such risks. It has been truly said time and again that the signing of a strict financial guarantee amounts to the same thing as signing or endorsing the applicant's note. About the only difference is that the bank usually charges six per cent. and secures collateral besides, while the surety company charges one per cent. and is not expected to demand collateral. I leave it to any one whether this is fair. For the very low rate charged the surety ought not to be expected to write this sort of guarantee unless fully protected and paid for the use of its name in extending credit. Many bonds of this nature are naturally declined by the home office, and then agents and applicants may become resentful, as they seem to think these bonds should be written on the same basis as a fire insurance company writes its policies. One of the most difficult things which you have to learn is to say, "No." Many agents have never learned this, and they will not be successful until they do.

Before submitting financial guarantee propositions to the home office for its consideration, if you are not sure that the financial statement of your customer is true, you should first make a thorough investigation yourself and send the result to the company. Always remember that we must assume that the litigation involved will be decided adversely to your applicant, and therefore, before the bond is executed, we must take every possible precaution to safeguard the surety against loss. This is particularly important, for the reason that *it is impossible to be released after a financial guarantee bond is once filed. Please remember that.* It is quite the opposite from fiduciary bonds, such as those for administrators, executors, guardians, etcetera, as a great majority of the States have through their legislatures enacted statutes by which in such cases a surety may be released.

BAIL BONDS HAZARDOUS.

Bail bonds are also considered very hazardous undertakings. They are conditioned for the delivery of the defendant, who has been accused of having committed a misdemeanor or crime, to the custody of the law at a time and place designated by the court. Very prominent citizens have been known to "skip their bail," as it is generally called, and even if afterward found, the expense to surety companies far exceeds the premium income. It is not safe to assume such liability without cash collateral. No other

kind of security should be considered sufficient, for the surety is called upon immediately to pay into court an amount equal to the penalty of the bond and then obliged to wait until some indefinite time when it may be reimbursed, if ever. As service of summons cannot be had in such matters, the time intervening, together with court costs and attorney fees, will cause an additional loss to the surety. I would advise you never to execute such a bond without the deposit of full cash collateral secured in advance.

On this class, as well as on any financial guarantee wherein collateral is necessary—never take real estate. Or, if you break that rule, never take real estate that is encumbered; and don't break this rule. It is better to take indemnity, if not an ultra vires act upon the part of the indemnitor, but the home office should decide this question—not you. For instance, when executing a financial guarantee bond for a corporation, you should always secure the indemnity of the officers and directors if collateral cannot be secured. If such personal indemnity is refused, it shows that those running the business are not acting in good faith—and, therefore, the bond should be declined. Of course, there are exceptions to this rule; but let the home office decide when there shall be an exception. Never take a mere outsider as a personal indemnitor, thinking you are making a bad risk look good. Such indemnity rarely, if ever, is any protection to the surety. You are almost always led into lawsuits, one on your bond and the other against your indemnitor. Even if this does not occur, your surety may be dead and his estate scattered to the four winds of heaven before the suit is settled, or if living he may have become insolvent, bankrupt or judgment proof.

It is unwise to depart from the underwriting standards followed by officials at the home office. Their rules are framed after long experience, and, as you know, experience is the best teacher.

THE HUMAN ELEMENT.

Wide Bonding Coverage—Varieties of Risks—Bond Fine Recommendation.

From the Fidelity Journal.

The fidelity bond is a commodity that is rapidly coming into general demand by the small as well as the large employers. This is doubly true since the surety companies have ceased to confine themselves to the payment of losses resulting strictly from acts of embezzlement. In the early years of the business, such acts were the only ones covered, but in recent years the companies have broadened the conditions of the coverage to losses arising through acts of fraud, dishonesty, larceny, embezzlement, wilful misapplication and wrongful abstraction, as well as continuing to write the old forms covering only larceny and embezzlement. These old forms are now practically confined to what they regard as the more hazardous risks; but, in nearly all cases at present where employees are working on the inside, or their duties are such that they do not actually handle money or securities, employers are able to secure bonds which will indemnify them against any loss that might be sustained as the result of an employee's personal dishonesty, or through his being dishonestly in collusion with others within or without the organization.

As a matter of fact, there is hardly any proposition which will be turned down to-day by a surety company. They are specializing in this line to such an extent that they will entertain any proposition demanding special coverage under employees' bonds, and in most instances are able to devise some way in which the desired coverage can be given, provided, it does not partake of the nature of a strictly financial guarantee. By thus broadening their protection they are able to be of much greater service to employers, and this service does not stop with the mere guarantee that they will reimburse employers for their losses sustained through the acts covered under the bonds.

CONFIDENCES KEPT.

There is a side to the fidelity business that is distinctly human, which is often made an instrument of service to an employer without his ever being aware of it. The surety companies often come into possession of information regarding an applicant, that if revealed to the employer through the same source, would prompt him to discharge or not employ one who

might oftentimes become a very valuable man. However, by having the surety company between him and loss, an employer often has a most capable employee whom he would not have if he had to take the same chance as the surety company.

The strange part of it is that the surety company does not consider that it is taking a chance. It assumes risks upon thousands of men, and it knows by experience that the losses that do occur are on men who have passed a most exhaustive investigation, and who, as the result of such investigation, any one would trust. With a bonding company it is always the trusted employee who goes wrong; otherwise, he would not be bonded. It also knows, however, that many men who have, on certain occasions and for certain reasons, been indiscreet and made mistakes, can, by proper handling, be brought back into the right path, and, moreover, it knows so well that if they do come back, it is willing, not so much to take a chance, but to give them a chance.

For example, the company with which the writer is connected, received, a short time ago, an application from a young married man who had to secure a new position, because his former employer had sold out his business. This man had charge of the closing out of the stock. Our investigation disclosed the fact that he had sold some of the stock for a certain price, remitted an amount less than the sale price, and pocketed the difference. Upon the company confronting him with the story, he admitted it. But, had his present employer known it, he, undoubtedly, would not have engaged him.

Further investigation showed that during the time that had elapsed between his leaving his old and applying for his new position he and his wife had gone to the country home of his boyhood days to stay with his parents, and by the time he made his application for bond there was a wife and child dependent upon him.

We then sent for him to call on us at our home office, and after a heart-to-heart talk, we told him that we would go on his bond, and sent him on his way rejoicing. We have watched his movements since, and that man has made good in his new position and will become an asset to the community, instead of the liability he would have become had he not been able to secure that position.

EMBARRASSING CIRCUMSTANCES.

In another case that stands out among many of like character, a man, also married, who had formerly led an exemplary life, became associated with some men in a concern in the West, which concern was threatened with destruction, unless more capital was secured. Through a scheme, too complicated to explain at length in this article, the capital was secured (by the

other men), and when the smoke cleared away our applicant was made a guest of the State for two years. Upon his release he came East and applied for a position. His prospective employer was one who makes it a rule to employ no one unless he can secure a bond.

The applicant was then, for the first time in his life, introduced to a bonding company, and, needless to say, the introduction brought about some mature reflection. In this case, the applicant opened up his past life to us. Upon investigation, we found that during the entire two years spent in the penitentiary his wife kept in constant touch with him, having secured a position near him, so that she could call on him as often as allowed. In order that he might live after his release, and until he could secure a position, she held hers, and sent him money enough to pay for his board and lodging.

Upon the completion of our investigation we sent for him to come to Baltimore. A half-hour chat with that man would convince even those inexperienced in the bonding business, that he had suffered the tortures of the damned. It developed that he was highly educated, was an expert accountant, good advertising man, and had the making of a capable business man and high-class citizen, if properly encouraged. We decided to bond him. He was given his position, and his employer was absolutely protected under his bond, but never knew that in his establishment there was being a real man made over, all on account of the human side of the fidelity business.

This man has since left his last employer, and now has a successful business of his own as consulting advertising specialist and expert sales writer. He and his wife are, of course, happily united again.

THE "POISON PEN."

A few years ago there came to us an anonymous letter giving most derogatory information regarding an employee we were bonding for a large sum. Ordinarily, anonymous letters should properly be ignored. In our business, however, when they cite specific information concerning an employee, and it agrees with that given in his application, it is wise from a fidelity underwriting viewpoint, to follow it up. While our underwriting side, however, said "cancel," the human side said "investigate." We did the latter. Our investigation, in addition to considerable correspondence and the use of our trained men in the field, also included the detailing of a special man to hunt down the source of the information, as well as to probe into the newly acquired habits and character of the employee.

This duty took our special investigator into the mining regions of the North in mid-winter, and after several days of traveling here and there, picking up threads of information, it developed

that the man in question had left his old home years before, had gone West, met with great success, and had become a most highly regarded citizen of his community. During an election for officers in a club to which he belonged, he had worked for the successful candidate, who was a personal friend of his, and the letter of information we received was inspired by the elected officer's opponent.

To the uninitiated, this may seem a trivial matter, but to a surety company it is far from it; otherwise, the expense involved in following up a case of his kind would never be incurred. It might occur to some readers that such matters are gone into in order to avoid a loss to the surety company. Such, however, is not the case. In all bonds executed on behalf of employees, a surety company reserves the right to cancel upon serving on the employer notice of cancellation, allowing a prescribed number of days after such notice before it becomes effective. Without a desire to do justice to the employee, or rather the desire not to do him an injustice, companies could avail themselves of this right immediately upon the receipt of adverse information regarding him.

So it goes. Incidents upon incidents like these could be cited showing the help and the lift given to some unfortunate who has been wrongfully accused, or who has actually strayed from the narrow path, and through the aid of the surety companies has come back. And such action is none the less helpful to the employer. There are many, of course, whom companies will not bond, as the exhaustive and thorough investigation to which they are subjected convinces them that they could not come back, but therein also lies the surety company's real service to employers. The fidelity bond, besides being a promise to pay, is easily the best recommendation an employer can require, and is likewise the best an employee can offer.

BACK TO THE NORMAL.

Revival of Bonding Business—Brokers' Blanket Bonds Hazardous.

By J. Frank Supplee, Resident Secretary, United States Fidelity and Guaranty Company.

The World's War is over—peace broods over the Nation—blest of God, America. It has been asserted that we are the luckiest people on earth, as we achieve our victories with the smallest loss of life and least expenditure of treasure. In the Spanish-American War we added to our domain, after a campaign of one hundred days, more territory than England secured in one hundred years of foreign conquest. We had under arms, in that war, about three hundred thousand men and suffered losses of less than fifty thousand from battle and disease. In this, the greatest war of all history, we had four and a half million men in our army and navy, and our casualties were about a quarter of a million, while Great Britain, with nine million in service, sustained losses of nearly one-third from all causes. Thanksgiving this year was celebrated by a grateful people, who realized that we are the pets of Providence.

From the contemplation of war risks, and war problems generally we take up cheerily the sentiment that peace hath her victories greater than war, and buckle down to normal thinking, working, and planning. In the department of finance and guarantee, for surety has always occupied a sort of no man's land between banking and insurance, we have come back to pre-war substantial methods.

NO MORE "JUMBO" BONDS.

In contract bonding, "the period of the emergency," the term used by the War Department, has ended, and there will be no more big bonds requiring reinsurance, some of them so huge as to require all of the combined underwriting power of the companies. Nature abhors a vacuum, science teaches, and we naturally look around for something to fill this aching void of lost war business. Happily, it has already appeared in the action of the various war boards in removing priorities and taking off the restrictions from building materials of all kinds. It is thought this will arouse the sleeping building trade that has been dormant for several years, and contract bonds will be required as the usufruct of this revival. Unfortunately, however, New

York investors do not seem to generally require bonds from builders or contractors.

There has been some interest of late in placing check-draft alteration indemnity policies. All the companies have canvassed the field, one company spending a lot of money in advertising and organizing a special force of solicitors for this propaganda. Some have asserted that the companies have not received a return in premiums of the amount expended. The legal fact that a bank cannot be held for a raised check if the signature is genuine operated to diminish the interest of the banks and they only required policies for the minimum amount. The average premium from the policies being five dollars also dampened interest in this new source of revenue.

HOLD-UPS RAMPANT.

The press reports the loss of $400,000 in cash and securities in the past month by messenger, hold-up and sneak thieves. The quick get-away of untried new messengers was the source of many losses. Liberty Bonds being as convertible as bank notes, seem to disappear as quickly as leaves in autumn. This has quickened interest in bankers' blanket bonds. and the companies writing them have been quite busy. Some new forms more liberal than ever have appeared on the market. They seem to cover every possible phase of destruction, mysterious disappearance and unlawful conversion and any other means by which securities fail to be secure.

This movement to give more liberal forms of coverage is a renaissance of the movement inaugurated about five years ago when all the surety companies were compelled by keen competition to revise and liberalize their bond forms. This movement happily eliminated the old requirement that larceny and embezzlement must be proven before the companies would pay loss. Some wag has asserted that the ultimate result of this competition as to forms would be the writing on a piece of paper of a bond reading, "for value received the Mammoth Surety Company, the greatest ever, hereby guarantees against any act causing loss," and leave a blank space for the assured to add any other language deemed fit to cover stealage, rottage, rust, or boll weevil.

The companies writing brokers' blanket bonds are scrutinizing very closely the moral hazard of applicants for protection. One company in its letter of instruction says, "We take this opportunity to state that we consider this form of bond even more hazardous than the bankers' blanket bond and intend to write them very conservatively, only issuing this bond for the large brokerage houses of unquestioned standing."

Recently the head of a large manufacturing company asked an officer of a surety company if he could suggest any way to pre-

vent infidelity and defalcation as he disliked to report so many losses under their schedule bond. The reply came very promptly that the situation reminded the surety man of the incident of the man who went into Harvey's restaurant, Washington, and said to the colored waiter, "Sam, have you a nice beefsteak about three inches wide, well cooked and so tender that it would melt in one's mouth?" "No, Boss, we ain't got no such steak; if we had Mr. Harvey would eat it hisself." The bond man added, "As we have suffered several defaults ourselves and jailed the offenders, collecting our losses from the surety company that bonds our employees, we know of no better form of protection than a good surety company."

It will be recalled that a leading company sustained a loss of at least a quarter of a million by the defalcation of a local officer some years ago and human nature seems to be the one unchangeable thing on this planet since its creation.

Despite the action of the American Bankers' Association at its convention at Chicago recently in tabling the project to do its own bonding, the New York Stock Exchange has a committee trying to evolve a scheme to issue a mutual bankers' blanket bond. Ignoring all the experience of the companies they seem to think a man may carry himself by his boot-straps without suspending the law of gravitation. There is said to be little chance of a successful fruition of the project.

DANGERS IN CONTRACT BONDING.

The Ætnaizer.

An outsider, with a new and unfamiliar point of view toward *your* work, may often disclose to you helpful ideas you have never thought of. Perhaps your business touches his at some point and the contact produces a spark that sheds light on both.

For example, a sub-contractor, who had had some costly experiences with general contractors to whom he was selling, unburdened himself recently concerning the irresponsibility of such general contractors. Furthermore, he was keen enough to see that any weakness of responsibility in a general contractor is a matter of great concern to a bonding company, just as it is to the sub-contractor, and that if the bonding company protects itself it will afford protection also to the sub-contractor.

Thus impelled to utterance, the sub-contractor voiced some excellent rules and principles for guidance in underwriting the bonds of general contractors, and these rules we here pass on for your benefit. If the ideas are new to you, we believe you will find them valuable; on the other hand, if you are already familiar with them, we believe you will find it worth while to refresh your memory. Here they are:

Bond should not be furnished where the general contractor is not rated in the first and second lines of credit, namely Dun and Bradstreet.

Any unsatisfactory dealings which a bonding company may have with an irresponsible general contractor should be reported immediately to Dun and Bradstreet.

Any concern which neither increases its capital or surplus nor pays dividends is surely losing money.

Any concern not carrying all kinds of liability insurance should not be bonded.

Any general contractor who does not issue "signed" financial statements every six or twelve months should not be bonded.

Millions of dollars are lost each year through selling on "supposed worth" or so-called "conservative worth."

We are going through a critical period; the questions are:

What are these general contractors going to pay for labor and materials, say three or six months from now?

What is their bonded indebtedness? And when is it due?

Have they ever paid a dividend? And what are the total dividends paid since commencing business?

How much will their several banks loan on their personal notes? And how much on their customers' notes?

Traveling in this direction, you will come to a State of Mind which is peaceful, and soon thereafter you will arrive within the gates of the City of Happiness.

UNDERWRITING CONTRACT BONDS.

Careful Examination of Financial Resources—Verification Necessary.

By John H. Davis, Chicago Bonding and Insurance Co.

As it is only the net surplus that constitutes the worth of a contractor, it is therefore very essential to exercise as much care in investigating the liabilities in order to ascertain their correctness as is used in checking up the assets. The liabilities usually consist of money borrowed from banks, mortgages on real estate, mortgages on plant and equipment, accounts payable, other liabilities, and in addition to the above capital stock, if the applicant should be a corporation. The investigation conducted at the bank will bring out information as to the applicant's indebtedness to the bank. The examination as to ownership of real estate should be conducted in such a manner as to ascertain what mortgages have been recorded against each piece. As to the accounts payable the applicant should furnish a detailed list of same, giving the names of persons or corporations to whom they are payable and dates on which they are due. These items should be verified as carefully as the accounts receivable. Care should also be taken to see whether the balance to be received from pending contracts will be sufficient to complete the contracts and pay all outstanding liabilities and leave a surplus or profit, a liberal allowance being made for contingencies. Another essential thing to be borne in mind in analyzing a financial statement is to see that the applicant's cash and good accounts receivable exceed his current liabilities, regardless of the value of real estate and other slow assets. When the items of bills payable and accounts payable are very large, it usually indicates that the applicant is doing more work than his finances justify. Mortgages on real estate often indicate that the applicant's borrowing power is limited. A chattel mortgage on the plant and equipment is almost sure sign of weakness, and applicant is not entitled to a bond.

The best time to secure a financial statement from a contractor is when he has little or no work on hand. A statement taken at a time when the applicant has any great amount of work on hand, as a rule, does not reflect the true condition. The cash on hand and accounts receivable may be in excess of the accounts payable, but there may be a large volume of outstanding bills not yet due and it may be impossible to complete

the pending work for the contract price. A condition of this kind you will readily appreciate would mean that the contractor was behind, when his statement might indicate that he was ahead.

We have learned from experience that contractors when they find themselves going behind on a contract put forth extra efforts to secure other work in the same vicinity, with a view of recouping their loss, or staving off failure, in the hope of future profits. Under the circumstances, a statement of accounts receivable and accounts actually due and payable may be accurate and may show ample resources, and yet the contractor may be insolvent.

We appreciate the possibility of some applicants strongly resenting the verification of their financial statement, and while this may come from some perfectly honest men, it will be generally found that those who seriously object are the ones who have made false statements. The general experience of the surety companies has been that in cases of default where the statement has not been verified the assets often prove to be fictitious. The only safe method to be followed in underwriting contract bonds is to give credence to only such assets shown in the financial statement as can be verified. It is vastly more important to verify the statements made by applicants for contract bonds than those of an applicant for a fidelity bond. A fidelity bond is rarely if ever executed until a thorough investigation of the applicant has been conducted. Is there any good reason for executing a contract bond, which is considerably more hazardous without doing so? Sentiment should never be allowed to enter into the underwriting of this class of business.

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